

Global Data Watch

- Global yields respond to rising growth and inflation forecasts
- Fed guidance remains vague on yields, is a potential source of volatility
- US outperformance a mixed bag for EM outlook
- Next week: Feb. global PMI rise, US job gain, Euro area HICP dip

Isn't she LVLY?

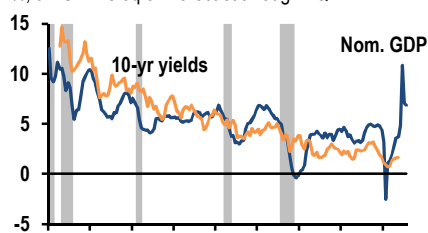
The year is young but has already produced a significant reassessment of the global outlook, prompted in part by expectations of substantial and sustained additional US fiscal stimulus. Beyond lifting our 2021 forecasts, the combination of a more-rapid-than-expected reduction of slack, increasing optimism on virus containment, and greater confidence in commitments for sustained policy support suggests that the global economy will sustain its reflationary tilt well beyond this year. We expect the US to be in the vanguard, and we now forecast US nominal GDP to average roughly 7% growth over this year and next (Figure 1). In this environment the US output gap is likely to close and core inflation to return to 2% sometime next year.

The positive interaction of fiscal and monetary policy stances is a key driver of the US's expected relative outperformance. The Fed is now committing to a sustained period in which inflation overshoots its target and is employing a low-for-very-long yield strategy (LVLY) to achieve its goal. To this end, it is using forward guidance to anchor policy rate expectations at the lower bound alongside balance sheet expansion to support low real bond yields. The thrust of these policies is to maintain market interest rates at a level accommodative enough to sustain strong growth and push inflation higher. US fiscal stimulus complements this effort by directly boosting growth. But the benefits of fiscal stimulus also come from enhancing the traction of LVLY policies as fiscal actions raise equilibrium real interest rates (r^*).

Against this backdrop, this year's 50bp rise in US 10-year yields is consistent with recent forecast changes, with the rise almost evenly split between inflation compensation and higher real yields. With yields still very low—both in absolute terms and in relation to the forecast—levels do not appear to pose a threat to US growth. While this week's Fed speakers echoed this view, the combination of dramatically shifting fundamentals and vague Fed guidance on its “slope” policies increases the potential for volatility in yields.

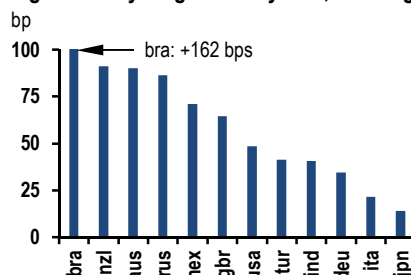
In contrast to the 2013 taper tantrum, there is little chance that yields will be

Figure 1: US nominal GDP and 10-yr yield
%, ar. GDP is 8q ch. forecast through 4Q22

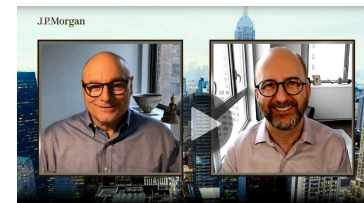


Source: J.P. Morgan

Figure 2: 10-year gov bond yields, YTD chg



Source: Bloomberg Finance L.P., J.P. Morgan



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pushed materially higher by muddled communication about the path of the Fed funds rate. Given the Fed's tolerance for an inflation overshoot and its guidance for liftoff, rate normalization is likely off the table at least through 2022. There is also the potential for considerable turnover on the FOMC, but the new appointment bias is likely to lean dovish.

However, anchoring short rates does not insure sustained low long-term yields, particularly if easy fiscal policy and a low-for-long Fed raises r^* and increases the risk of higher inflation. The Fed's vague guidance on its tolerance for rising yields could thus be a problem, even as it is understandable given difficulties in measuring r^* and its desire to boost inflation expectations. What's more, the parameters for calibrating balance sheet policy are not well established. Decisions on this front incorporate considerations about financial stability and macroeconomic objectives that look set to lean in different directions in the coming quarters. At present, we see the Fed announcing a tapering program that starts early next year.

Rest of world eyes US yield rise warily...

With the US recovery expected to outpace the rest of the world, including China, in coming quarters, the fallout from rising US rates on global financial markets raises tensions. With the Euro area in the midst of a second consecutive quarter of contraction and underlying inflation anticipated to remain well below the target for some time, ECB commentary is striking a different note to the Fed's. Speakers emphasize that the increase in bond yields is being monitored "closely" and that there is flexibility in PEPP to respond. However, it is not clear that this reflects anything more than jawboning. ECB chief economist Lane spoke about a new "compass" this week, whereby the ECB insures favorable financing conditions to support the economy. But he also noted the ECB is not engaged in yield curve control and that staff forecasts are important in deciding whether market moves are unwarranted. With the staff expected to revise up its inflation forecast despite the rise in yields in March, it is unclear that any action will be forthcoming.

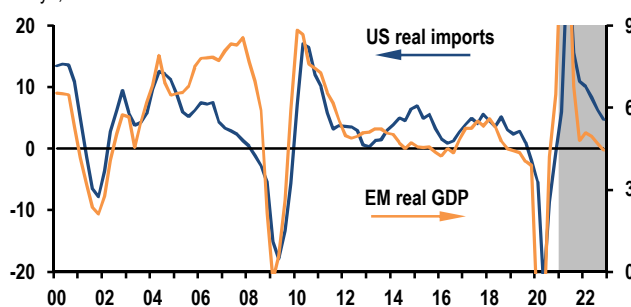
...with mixed reaction in EM Asia...

Lending rates have also tightened in EM over the past few weeks alongside heightened market expectations of global reflation (Figure 2). Although expected, the attendant rise in EM interest rates, especially among some of the high-yielders (e.g., Brazil, India, and Indonesia) has been exacerbated by concerns over a repeat of the EM financial instability during the 2013 taper tantrum. [We do not think EM economies are vulnerable](#) in the same way they were in 2013, in part because there is little sign of overheating and external imbalances are virtually absent this time around. To the extent that this rise in rates reflects higher global growth, the boost to EM activity

should dominate the drag from higher interest rates (Figure 3). This is particularly true for the tech producers in North Asia. In Korea, we recently upgraded our 2021 full-year GDP growth to 4.0%, on a higher global growth forecast and a stronger-than-expected 4Q20 GDP outcome. This projection implies core price inflation firming to above a 1.5% pace. Combined with concerns around elevated household leverage, we now see the BoK hiking in 1Q22.

Figure 3: US imports and EM GDP

%o/y; both scales



Source: J.P. Morgan

For current account deficit countries in EM Asia, the dynamics are complicated by a need to maintain external financing in a world of more attractive US rates. This is exacerbated by deteriorating terms of trade for net importers of commodities. Rising oil prices and a robust recovery are expected to push India back into a 1% current account deficit this year. While we still look for a balance of payments surplus, it will be lower and provide less support for domestic bonds as private savings retreat relative to investment needs. This, in turn, is already contributing to rising rates. In Indonesia, commodity price gains will not offset a rising investment-saving gap that is expected to deepen the current account deficit to 1.2% of GDP this year. Funding for this deficit could get a fillip later this year as reforms related to the Omnibus law catalyze FDI inflows. In the meantime, higher rates are required and yields have been on the rise.

...and adding to hawkish shift in EMEA EM

The recent rise in US rates adds to already hawkish leaning across EMEA EM, particularly for the high-yielding economies of Russia, Turkey, and South Africa. Russia's CBR now talks about the possibility of hikes this year (we see it in 1Q22), while Turkey's CBRT hiked reserve requirements by 200bp this week. The move was designed to temper banks' appetite to lend, but it likely also was a response to the recent tightening in global market conditions that complicates financing of a wide CA deficit. We have seen a shift among low-yielders as well. Czechia's CNB dialed up its hawkish tone, while the Polish and Romanian central banks have stopped talking about easing. We

have removed the 15bp rate cut we had in 3Q21 for Hungary and, given contradictory policy goals, see increasing risks of the market forcing the NBH to tighten monetary conditions. In Romania we still have a 25bp rate cut over the next few months, but its likelihood has fallen sharply against very strong 4Q20 growth and global developments.

Fiscal dynamics also in EM CB thinking

Fiscal policy considerations also influence EM central bank thinking. This week we changed our Brazil outlook significantly: not only because of tighter global financial conditions, but also because of rising uncertainty over policy management. Financial stability concerns were amplified late last week with President Bolsonaro's sudden replacement of the Petrobras CEO following fuel price hikes and threats of a truckers' strike. The recent turbulence, combined with the rise in commodity prices that led us to revise up our inflation forecast, requires tighter monetary policy. We now call for a 50bp COPOM hike in March.

In South Africa, the improving terms of trade from rising commodity prices is complemented by enhanced policy credibility. The resulting pickup in corporate tax receipts will dampen fiscal stress. At this week's FY21/22 budget presentation, the authorities marked up the revenue outlook and we see upside risk to it. In addition, the political signal for structural reforms was much stronger than expected. For the SARB, which has long been concerned about fiscal vulnerabilities, recent developments take some pressure off. However, with growth on the mend and a quick closing of the output gap, we still see a second hike in 1H22 with some risk (25%) that the SARB may begin to tighten this year.

Best-laid plans of policymakers and economists

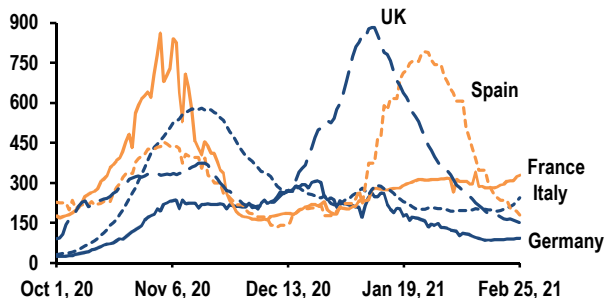
After a modest soft patch that will slow global growth to just below its potential this quarter, the outlook turns decisively brighter with a projected 7.7% ar global GDP boom through 2Q and 3Q, followed by a robust 3.6% ar gain for the next five quarters. The forecast for 2021-22 as a whole looks for the strongest two years of growth in half a century. While this upbeat forecast rests on many moving parts, a central feature is the dissipation of the pandemic as a material macroeconomic headwind. The latest developments point to easing restrictions, rising mobility, and improving vaccinations, but risks linger—particularly with regard to new variants.

In Europe, the second wave has had the biggest impact on growth, and countries with the most severe restrictions in place are under pressure to ease. This week saw the UK lay

out a path toward the removal of most of its measures by the end of June. If the forecast is tracking, we would expect to see a broad-based European upturn in mobility and a bounce in business surveys through March. However, even as case counts continue to slide in much of Europe, [France](#) and [Italy](#) reported renewed rises in caseloads that spark concern of a variant-driven third wave and resulted in renewed lockdowns in Paris and the Lombardy region (Figure 4). While the evidence has yet to clearly point to a new variant that is able to evade existing vaccines, it remains a material risk.

Figure 4: COVID-19 new cases

Per million, 7d m.a.



Source: J.P. Morgan, Our World in Data

NPC to unveil macro targets next week

Policymakers in China are navigating a difficult course. A boom in global goods demand is fueling a surge across export industries, while the real estate and infrastructure sectors are overheating. At the same time, concerns around a domestic second wave soft patch, alongside disappointing January business surveys, have motivated policymakers to allow credit growth to run strong into the new year. Higher-frequency data have been encouraging, but we maintain a cautious stance for next week's February survey readings. We expect the NBS PMI to tick lower and the IHS/Markit reading to hold steady.

Policymakers will have a chance to articulate their goals at next week's annual National People's Congress (March 5), which will approve the government's work report for 2021 and the 14th Five-Year Plan (FYP, 2021-2025). While the general principles were laid out in the Central Economic Work Conference (CEWC) in December and the Party's 5th Plenum in October, next week's publication will detail numerical targets. We expect the quota of government bond issuance will be reduced to 6.4tn yuan (6.4% of GDP) this year from 8.5tn yuan (8.5% of GDP) in 2020, the inflation target will be lowered from 3.5% in 2020 to 3%, and money supply and TSF growth will be in line with 11.6% nominal GDP growth for 2021.

Global economic outlook summary

	Real GDP			Real GDP						Consumer prices			
	% over a year ago			% over previous period, saar						% over a year ago			
	2020	2021	2022	2Q20	3Q20	4Q20	1Q21	2Q21	3Q21	2Q20	4Q20	2Q21	4Q21
United States	-3.5	6.2	4.0	-31.4	33.4	4.1↑	<u>5.0</u>	9.5	8.3	0.4	1.2	3.4↑	2.6↑
Canada	-5.4	5.2↑	4.5↑	-38.1	40.5	<u>7.6</u>	-2.0	9.5	8.0	0.0	0.8	2.8	2.3
Latin America	-6.7	4.8↑	3.2	-43.8↑	51.8↑	15.6↑	-3.4↓	4.8↑	4.4↑	6.5	6.7	9.7↑	9.0↑
Argentina	-10.0	5.8	1.7	-50.2	61.7	<u>20.0</u>	0.0	1.0	2.0	43.8	36.3	53.5	55.0
Brazil	-4.3	3.1↑	2.4↓	-33.2	34.6	<u>10.0</u>	-5.0	3.5↑	4.0↑	2.1	4.3↓	6.8↑	5.1↑
Chile	-6.0	5.9↑	3.2↑	-43.9	22.6	<u>27.7</u>	2.0	4.0↑	4.0	2.9	3.0	4.0	3.5
Colombia	-6.8	5.8	4.8	-47.3	43.1	26.5	<u>-2.0</u>	6.0	4.0	2.9	1.6	1.6	2.5
Ecuador	-7.2	2.8	1.9	-36.2	19.3	<u>8.0</u>	3.2	2.5	2.5	0.6	-1.1	-1.6	0.3
Mexico	-8.2↑	5.6↑	4.1↑	-52.1↑	59.6↑	13.7↑	-2.1↑	9.5↑	6.4↑	2.8	3.5	4.2↑	3.3↑
Peru	-11.1↑	9.9↓	6.1↑	-70.4↑	195.3↑	38.1↑	-16.0↓	-1.0↓	5.0↑	1.7	2.2↑	2.0	1.9
Uruguay	-5.7	2.8	3.0	-35.5	35.2	<u>8.0</u>	0.0	0.5	2.7	10.8	9.7	6.9	7.1
Asia/Pacific	-1.2↓	7.8↑	4.7	8.8	24.9↑	13.6↓	4.6↑	5.0↑	5.6↑	2.0	0.6	1.2	1.9↑
Japan	-4.9	4.1↑	2.4↓	-29.3	22.7	12.7	-1.0↑	5.0↓	5.0↓	0.1	-0.8	-0.4↑	0.4↑
Australia	-2.9	3.8↑	3.0↑	-25.3	14.0	<u>6.6</u>	4.6↓	5.1↑	4.0↑	-0.3	0.4	2.9	2.0
New Zealand	-3.3	2.8↑	4.6↑	-37.4	68.9	<u>-8.9</u>	-4.5	5.3↑	6.8↑	1.5	0.9	1.2	1.5
EM Asia	-0.3↓	8.9	5.3	20.0	25.6↑	14.4↓	5.9↑	5.0↑	5.8↑	2.6	1.0	1.5	2.2
China	-2.3	9.4	5.6	54.7	7.1	14.9	<u>6.0</u>	4.5	5.5	2.7	0.1	0.7	2.0
India	-8.0↓	13.2↓	4.3↓	-68.5↓	118.9↑	24.7↓	11.0↑	6.5↑	6.0↑	6.5	6.4	4.3	3.8
Ex China/India	-2.8	5.1↓	5.1↑	-22.2	23.0↑	7.5↓	2.9↓	5.7↑	6.4↑	0.1	0.5	2.1↑	2.0↑
Hong Kong	-6.1	5.2↑	3.6↑	-0.4	11.2	0.8	3.9↑	8.0↑	7.2	1.3	-0.3	1.1↑	2.6↑
Indonesia	-2.1	5.0↓	4.8	-24.9	14.1	10.7	4.0↓	6.0↑	5.0	2.3	1.6	1.7	2.1
Korea	-1.0	4.0	4.4	-12.0	8.8	4.4	<u>3.0</u>	4.0	9.0	-0.1	0.4	1.9	1.9
Malaysia	-5.6	6.8	4.9	-51.4	95.3	-1.0	<u>2.5</u>	9.0	5.0	-2.6	-1.5	2.8	1.9
Philippines	-9.5	7.0	5.7	-47.5	36.1	24.2	<u>3.6</u>	5.3	5.3	2.3	3.1	4.7	3.6
Singapore	-5.4	5.7	8.0	-43.0	41.0	15.9	<u>1.0</u>	5.0	3.0	-1.2	-0.1	0.9	0.7
Taiwan	3.1↑	6.2↑	3.6↑	-2.9↓	18.5↑	5.8↓	4.0↑	6.2↑	6.0↑	-1.0	0.0	1.8↑	1.8↑
Thailand	-6.1	4.3	7.8	-32.7	27.3	5.4	<u>0.0↓</u>	6.2↑	5.0↑	-2.7	-0.4	3.1	1.3
Western Europe	-7.1	5.6	5.1	-41.4	61.6↑	-1.1↓	-3.1↑	14.6↓	9.8	0.3	-0.1	1.9↑	2.3
Euro area	-6.8	5.7	4.8	-39.2	59.9	-2.4	<u>-1.0</u>	13.0	8.5	0.2	-0.3	1.9↑	2.3
Germany	-5.3	4.7↑	4.6	-33.5	38.6	1.4↑	<u>-5.0</u>	17.5	7.0	0.7	-0.6	2.6↑	3.8↑
France	-8.2↑	7.3↓	4.0	-44.0↑	96.9↓	-5.7↓	<u>4.5</u>	8.0	6.0	0.3	0.1	1.5	1.5
Italy	-8.9	6.3	5.3	-42.8	80.9	-7.7	<u>1.5</u>	11.0	10.0	-0.2	-0.4	1.0	1.5
Spain	-11.0	6.6	7.4	-54.5	83.7	1.6	<u>-2.0</u>	10.0	15.0	-0.6	-0.8	2.1↑	2.7↑
Norway	-3.1	4.1	3.4	-21.7	21.6	7.8	<u>-0.5</u>	5.0	5.5	1.1	1.3	2.4↑	2.6↑
Sweden	-3.0	3.3↑	3.7	-27.0↑	28.3↑	-1.0↓	-0.5↑	7.5↓	6.5	0.1	0.6	1.9	1.2
United Kingdom	-9.9	5.6	7.1	-57.0	81.9	4.0	<u>-14.0</u>	25.0	17.2	0.7	0.6	2.1	2.4
EMEA EM	-2.7	4.2	4.0	-33.0	41.2	<u>5.2</u>	-0.2	5.3↑	4.4↑	4.1	4.9	5.5	4.8
Czech Republic	-5.7	4.7	5.2	-29.9	30.8	1.2	<u>1.5</u>	8.0	8.0	3.1	2.6	1.9	2.0
Hungary	-5.2	5.2	6.0	-46.8	53.9	4.5	<u>-2.5</u>	9.5	8.5	2.5	2.8	3.7	3.7
Israel	-2.3	6.6	5.5	-29.9	41.5	6.3	<u>2.8</u>	8.7	5.7	-1.1	-0.7	0.9	1.0
Poland	-2.7	4.2	6.1	-25.2	35.5	-2.8	<u>-0.9</u>	9.8	8.7	3.2	2.8	2.5	3.0
Romania	-3.9	6.0	6.5	-40.6	26.7	22.9	<u>-2.5</u>	6.1	9.5	2.5	2.1	2.9	3.7
Russia	-3.1	3.1	2.8	-29.0	24.0	<u>2.3</u>	2.0	5.5	3.0	3.1	4.5	4.7	4.0
South Africa	-6.7	4.3↑	2.2	-51.7	66.1	<u>12.0</u>	-1.5	3.0↑	2.0↑	2.4	3.2	4.6	4.1
Turkey	1.9	4.6	3.3	-36.6	78.4	<u>10.0</u>	-4.7	-1.6	0.8	11.7	13.5	14.8	11.7
Global	-3.6	6.4	4.5	-19.6	38.1↑	7.3↓	2.1↑	8.5↑	7.1↑	1.5	1.2	2.8↑	2.8↑
Developed markets	-5.0	5.7↑	4.2	-34.9	42.4↑	<u>3.3</u>	1.1↑	10.7↓	8.3↓	0.3	0.5	2.4↑	2.2↑
Emerging markets	-1.5↓	7.6	4.8	3.2	31.6↑	13.3↓	3.7	5.0↑	5.4↑	3.4	2.4	3.3↑	3.6↑
Emerging ex China	-4.7↓	6.2↑	4.2	-38.5	51.5↑	12.0↓	1.9↑	5.5↑	5.3↑	2.4	2.6	2.9↑	2.6↑
Global — PPP weighted	-3.4↓	7.0	4.5↓	-18.4	39.4↑	8.9↓	3.0↑	7.9↑	6.8↑	2.0	1.6	2.7↑	2.7↑

Note: For some emerging economies seasonally adjusted GDP data are estimated by J.P. Morgan. Bold denotes changes from last edition of *Global Data Watch*, with arrows showing the direction of changes. Underline indicates beginning of J.P. Morgan forecasts. Unless noted, concurrent nominal GDP weights calculated with current FX rates are used in computing our global and regional aggregates. Regional CPI aggregates exclude Argentina and Ecuador. Source: J.P. Morgan. Any long-form nomenclature for references to China; Hong Kong; and Taiwan within this research material is Mainland China; Hong Kong SAR (China) and Taiwan (China).

G-3 economic outlook detail

				2020			2021				2022
	2020	2021	2022	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q
United States											
Real GDP	-3.5	6.2	4.0	-31.4	33.4	4.1	5.0	9.5	8.3	3.0	3.5
Private consumption	-3.9	7.2	4.3	-33.2	41.0	2.4	5.3	11.5	9.5	5.8	2.8
Equipment investment	-5.0	16.8	6.1	-35.9	68.2	25.7	19.0	10.0	9.0	9.0	6.0
Non-residential construction	-10.6	-3.8	6.4	-33.6	-17.4	1.1	-2.0	3.0	5.0	6.0	8.0
Intellectual property products	1.6	6.9	8.5	-11.4	8.4	8.4	7.0	9.0	9.0	9.0	9.0
Residential construction	6.0	19.4	6.2	-35.6	63.0	35.8	20.0	14.0	12.0	7.0	5.0
Inventory change (\$ bn saar)	-80.9	115.4	60.6	-287.0	-3.7	48.0	53.1	116.3	189.0	103.2	87.6
Government spending	1.1	-0.4	4.6	2.5	-4.8	-1.1	-0.2	0.4	0.4	3.4	6.9
Exports of goods and services	-13.0	5.9	4.8	-64.4	59.6	21.8	6.3	4.2	4.4	4.3	5.5
Imports of goods and services	-9.3	15.5	7.3	-54.1	93.1	29.6	10.0	12.0	12.0	10.0	6.5
Domestic final sales contribution	-2.6	6.6	4.8	-28.5	30.1	4.5	5.9	9.8	8.3	6.0	4.4
Inventories contribution	-0.7	1.0	-0.3	-3.5	6.6	1.1	0.1	1.3	1.5	-1.7	-0.3
Net trade contribution	-0.2	-1.4	-0.5	0.6	-3.2	-1.6	-1.0	-1.6	-1.6	-1.3	-0.6
Consumer prices (%oya)	1.3	2.6	2.1	0.4	1.3	1.2	1.8	3.4	2.7	2.6	2.2
Excluding food and energy (%oya)	1.7	1.7	2.1	1.3	1.7	1.6	1.4	2.2	1.6	1.7	1.9
Core PCE deflator (%oya)	1.4	1.8	1.8	1.0	1.4	1.4	1.6	2.2	1.7	1.8	1.6
Federal budget balance (% of GDP, FY)	-15.0	-16.3	-9.9								
Personal saving rate (%)	16.1	14.4	7.4	26.0	15.7	13.0	20.7	16.7	12.9	7.5	7.3
Unemployment rate (%)	8.1	5.2	3.8	13.1	8.8	6.8	6.2	5.4	4.8	4.5	4.1
Industrial production, manufacturing	-6.7	6.8	2.8	-46.5	56.3	11.2	3.0	8.0	5.8	2.8	2.0
Euro area											
Real GDP	-6.8	5.7	4.8	-39.2	59.9	-2.4	-1.0	13.0	8.5	5.5	4.0
Private consumption	-8.0	4.6	4.8	-41.2	68.5	-12.0	1.0	10.0	12.0	5.0	3.5
Capital investment	-9.1	3.9	6.3	-50.0	66.8	-9.0	2.0	8.0	10.0	10.0	5.0
Government consumption	1.1	4.5	2.1	-8.6	20.8	5.0	3.0	3.0	2.0	2.0	2.0
Exports of goods and services	-10.4	7.5	4.6	-56.8	85.9	3.0	2.0	14.0	11.0	3.0	3.0
Imports of goods and services	-10.0	5.7	4.9	-55.2	58.6	3.0	2.0	15.0	10.0	3.0	3.5
Domestic final sales contribution	-6.1	4.2	4.3	-34.8	55.1	-7.7	1.6	7.9	8.7	5.1	3.3
Inventories contribution	-0.1	0.5	0.4	-0.9	-5.0	5.2	-2.7	5.0	-1.0	0.3	0.8
Net trade contribution	-0.6	1.0	0.1	-3.6	9.7	0.1	0.1	0.2	0.8	0.1	-0.1
Consumer prices (HICP, %oya)	0.3	1.9	1.1	0.2	0.0	-0.3	1.1	1.9	2.1	2.3	1.1
ex food, alcohol and energy	0.7	1.3	1.0	0.9	0.6	0.2	1.1	1.1	1.3	1.6	0.9
General govt. budget balance (% of GDP, FY)	-9.2	-6.5	-3.7								
Unemployment rate (%)	8.0	8.9	8.6	7.6	8.6	8.3	8.8	8.9	8.9	8.9	8.8
Industrial production	-8.4	8.0	4.0	-49.7	82.9	16.6	0.0	5.0	5.0	5.0	4.0
Japan											
Real GDP	-4.9	4.1	2.4	-29.3	22.7	12.7	-1.0	5.0	5.0	3.0	2.0
Private consumption	-6.0	3.1	2.9	-29.5	22.0	8.9	-4.0	7.0	6.0	4.0	2.5
Business investment	-6.0	3.3	5.2	-21.5	-9.2	19.4	3.0	2.0	9.0	8.0	5.0
Residential construction	-7.0	-1.7	1.0	2.0	-21.0	0.2	3.0	1.0	1.0	1.0	1.0
Public investment	3.6	3.0	0.8	9.2	3.6	5.5	1.0	2.0	2.0	2.0	1.0
Government consumption	2.7	3.4	-0.4	0.9	11.7	8.1	2.0	0.0	0.0	0.0	0.0
Exports of goods and services	-12.4	13.9	7.8	-52.9	33.2	52.3	10.0	10.0	15.0	10.0	8.0
Imports of goods and services	-6.8	5.0	9.4	5.1	-29.0	17.3	6.0	10.0	15.0	15.0	10.0
Domestic final sales contribution	-3.8	3.1	2.4	-17.9	12.4	10.0	-1.1	4.2	4.7	3.5	2.2
Inventories contribution	0.0	-0.4	0.2	1.3	-1.4	-1.9	-0.6	0.8	0.2	0.2	0.1
Net trade contribution	-1.1	1.5	-0.2	-12.6	11.8	4.6	0.7	0.1	0.1	-0.8	-0.3
Consumer prices (%oya)	0.0	-0.1	0.2	0.1	0.2	-0.8	-0.4	-0.4	0.1	0.4	0.0
ex food and energy	-0.1	-0.2	-0.2	0.0	-0.1	-0.5	0.0	-0.8	-0.1	0.0	-0.2
General govt. net lending (% of GDP, CY)	-11.5	-10.8	-6.3								
Unemployment rate (%)	2.8	3.0	2.8	2.8	3.0	3.0	3.1	3.0	3.0	2.9	2.9
Industrial production	-10.3	11.3	3.1	-52.3	39.9	26.8	15.5	11.0	10.0	2.0	2.0
Memo: Global industrial production	-5.4	8.8	3.8	-25.6	69.1	12.1	4.0	6.6	5.9	3.9	0.0
%oya				-13.9	-3.6	-0.4	4.1	19.0	7.0	5.0	0.0

Note: More forecast details for the G-3 and other countries can be found on J.P. Morgan's Morgan Markets client web site. Source: J.P. Morgan

Global Central Bank Watch

	Official rate	Current rate (%pa)	4-qrtr change (bp)		Last change	Next mtg	Forecast next change	Forecast (%pa)				
			Last	Next				Mar 21	Jun 21	Sep 21	Dec 21	Mar 22
Global		1.18	-84	-1				1.16	1.17	1.18	1.18	1.18
excluding US		1.53	-40	-2				1.51	1.52	1.54	1.53	1.54
Developed		-0.02	-97	0				-0.02	-0.02	-0.02	-0.02	-0.02
Emerging		3.02	-70	-3				2.99	3.00	3.04	3.03	3.04
Latin America		2.41	-242	15				2.56	2.95	3.44	3.97	4.21
EMEA EM		4.92	-21	-1				4.91	4.91	4.74	4.24	4.01
EM Asia		2.75	-49	-6				2.68	2.62	2.62	2.62	2.64
The Americas		0.56	-163	2				0.59	0.64	0.71	0.79	0.83
United States	Fed funds	0.25	-150	0	15 Mar 20 (-100bp)	17 Mar 21	On hold	0.25	0.25	0.25	0.25	0.25
Canada	O/N rate	0.25	-150	0	27 Mar 20 (-50bp)	<u>3 Mar 21</u>	On hold	0.25	0.25	0.25	0.25	0.25
Brazil	SELIC O/N	2.00	-225	50	5 Aug 20 (-25bp)	17 Mar 21	Mar 21 (+50bp)	2.50	3.50	4.50	5.50	6.00
Mexico	Repo rate	4.00	-298	-25	11 Feb 21 (-25bp)	25 Mar 21	Mar 21 (-25bp)	3.75	3.50	3.50	3.50	3.50
Chile	Disc rate	0.50	-125	0	31 Mar 20 (-50bp)	30 Mar 21	4Q 21 (+25bp)	0.50	0.50	0.50	0.75	0.75
Colombia	Repo rate	1.75	-250	0	25 Sep 20 (-25bp)	26 Mar 21	3Q 21 (+25bp)	1.75	1.75	2.00	2.50	2.50
Peru	Reference	0.25	-200	0	9 Apr 20 (-100bp)	11 Mar 21	1Q 22 (+25bp)	0.25	0.25	0.25	0.25	0.50
Europe/Africa		0.72	-38	0				0.72	0.72	0.68	0.58	0.54
Euro area	Depo rate	-0.50	0	0	12 Sep 19 (-10bp)	11 Mar 21	On hold	-0.50	-0.50	-0.50	-0.50	-0.50
United Kingdom	Bank rate	0.10	-65	0	19 Mar 20 (-15bp)	18 Mar 21	On hold	0.10	0.10	0.10	0.10	0.10
Norway	Dep rate	0.00	-150	0	7 May 20 (-25bp)	18 Mar 21	1Q 22 (+25bp)	0.00	0.00	0.00	0.00	0.25
Sweden	Repo rate	0.00	0	0	19 Dec 19 (+25bp)	27 Apr 21	On hold	0.00	0.00	0.00	0.00	0.00
Czech Republic	2-wk repo	0.25	-200	0	7 May 20 (-75bp)	24 Mar 21	4Q 21 (+25bp)	0.25	0.25	0.25	0.50	0.50
Hungary	Base rate	0.60	-30	0	21 Jul 20 (-15bp)	23 Mar 21	On hold	0.60	0.60	0.60	0.60	0.60
Israel	Base rate	0.10	-15	0	6 Apr 20 (-15bp)	19 Apr 21	On hold	0.10	0.10	0.10	0.10	0.10
Poland	7-day interv	0.10	-140	0	28 May 20 (-40bp)	<u>3 Mar 21</u>	4Q 22 (+15bp)	0.10	0.10	0.10	0.10	0.10
Romania	Base rate	1.25	-125	-25	15 Jan 21 (-25bp)	-	Mar 21 (-25bp)	1.00	1.00	1.00	1.00	1.00
Russia	Key pol rate	4.25	-175	0	24 Jul 20 (-25bp)	19 Mar 21	1Q 22 (+25bp)	4.25	4.25	4.25	4.25	4.50
South Africa	Repo rate	3.50	-275	0	23 Jul 20 (-25bp)	25 Mar 21	Mar 22 (+25bp)	3.50	3.50	3.50	3.50	3.75
Turkey	1-wk repo	17.00	625	0	24 Dec 20 (+200bp)	18 Mar 21	3Q 21 (-100bp)	17.00	17.00	16.00	13.00	11.00
Asia/Pacific		2.10	-42	-6				2.05	2.00	2.00	2.00	2.01
Australia	Cash rate	0.25	-50	-15	19 Mar 20 (-25bp)	<u>2 Mar 21</u>	On hold	0.10	0.10	0.10	0.10	0.10
New Zealand	Cash rate	0.25	-75	0	15 Mar 20 (-75bp)	14 Apr 21	Nov 21 (-25bp)	0.25	0.25	0.25	0.00	0.00
Japan	Pol rate IOER ¹	-0.10	-9	0	28 Jan 16 (-20bp)	19 Mar 21	On hold	-0.10	-0.10	-0.10	-0.10	-0.10
Hong Kong	Disc. wndw	0.50	-150	0	3 Mar 20 (-50bp)	-	On hold	0.50	0.50	0.50	0.50	0.50
China	1-yr MLF	2.95	-20	-10	15 Apr 20 (-20bp)	-	1Q 21 (-10bp)	2.85	2.75	2.75	2.75	2.75
Korea	Base rate	0.50	-75	0	28 May 20 (-25bp)	15 Apr 21	1Q 22 (+25bp)	0.50	0.50	0.50	0.50	0.75
Indonesia	BI RRR	3.50	-125	0	18 Feb 21 (-25bp)	18 Mar 21	On hold	3.50	3.50	3.50	3.50	3.50
India	Repo rate	4.00	-115	0	22 May 20 (-40bp)	7 Apr 21	On hold	4.00	4.00	4.00	4.00	4.00
Malaysia	O/N rate	1.75	-100	0	7 Jul 20 (-25bp)	<u>4 Mar 21</u>	On hold	1.75	1.75	1.75	1.75	1.75
Philippines	Rev repo	2.00	-175	0	19 Nov (-25bp)	25 Mar 21	On hold	2.00	2.00	2.00	2.00	2.00
Thailand	1-day repo	0.50	-50	0	20 May 20 (-25bp)	24 Mar 21	On hold	0.50	0.50	0.50	0.50	0.50
Taiwan	Official disc.	1.125	-25	0	19 Mar 20 (-25bp)	18 Mar 21	On hold	1.13	1.13	1.13	1.13	1.13

Source: J.P. Morgan. ¹ BoJ sets the policy rate on IOER (O/N) and targets 10-year JGB yields as policy guidance. Bold denotes move since last GDW and forecast changes. Underline denotes policy meeting during upcoming week. Aggregates are GDP-weighted averages. Any long-form nomenclature for references to China; Hong Kong; and Taiwan within this research material is Mainland China; Hong Kong SAR (China) and Taiwan (China).

Nowcast global GDP 1Q: Tracking early upside risk

Early-year data signal upside risk to our 1Q global growth forecast. While we have made significant revisions to the US outlook in recent weeks, upside risks remain according to our US nowcast (Figure 1). At the same time, upside revisions to the US have yet to trigger the usual response in rest-of-world forecasts. With US real imports now projected to surge over 10% this year, there is considerable impulse to go around. Notably, our country nowcasts echo the message of broad-based upside risk. On balance, we forecast global GDP to expand at a soft 2.1% ar his quarter, but see growth roaring back over the remainder of the year. We will learn more next week when we see the full global set of February PMIs. The available DM flash PMI reports came in positive with a modest increase on the month.

Figure 1: J.P. Morgan global GDP

% change saar

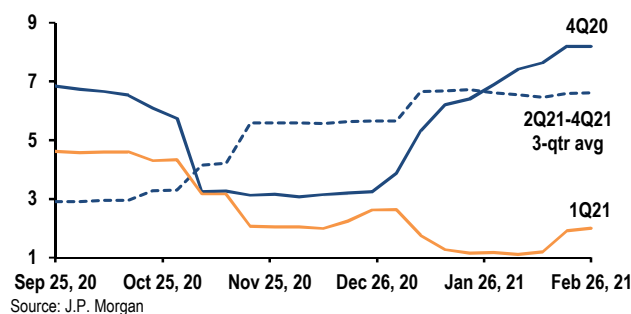
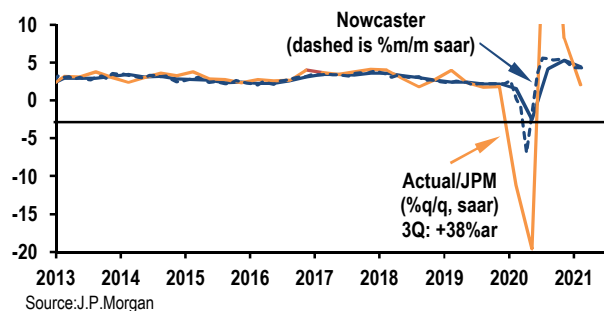


Figure 2: Global real GDP

%q/q, saar; J.P. Morgan projection and Nowcaster through 1Q21



Our top-down global nowcaster for tracking 1Q global growth stood at 4.5% ar (Figure 2) again this week, a much stronger reading than our official forecast, even after recent revisions that raised our current-quarter forecast by 0.9% ar over the past three weeks. The nowcaster sent the right signal of upside risk through all of 4Q20. Running counter to the strong global nowcaster, the aggregate of our bottom-up nowcasters remains below the official forecast with a reading of 1.3% ar (Table 1). The majority of our country-level nowcasters sug-

gest upside risk. Our nowcaster for China is a notable outlier and points to a 1% ar contraction this quarter against our forecast for a 6% ar gain. The risk bias in the US and Euro area is roughly neutral (Figure 3).

Table 1: Real GDP

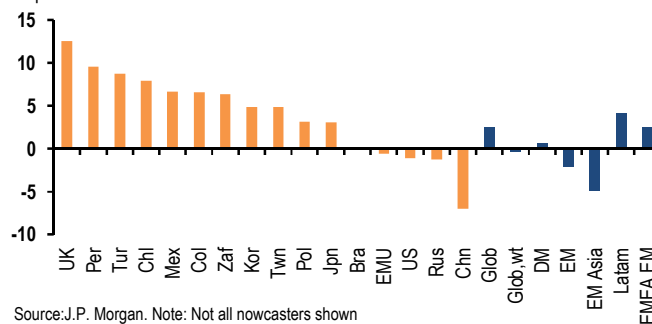
%q/q, saar. Underline indicates J.P. Morgan forecast

	4Q20		1Q21	
	Actual/Fcst	Nowcast	Forecast	Nowcast
Global	<u>8.2</u>	5.3	<u>2.0</u>	4.5
Weighted Avg*	<u>6.6</u>	7.0	<u>1.7</u>	1.3
Developed*	<u>3.2</u>	5.6	<u>1.0</u>	1.7
US	4.1	7.6	<u>5.0</u>	3.9
EMU	-2.4	1.4	<u>-1.0</u>	-1.6
UK	<u>4.0</u>	-1.2	<u>-14.0</u>	-1.5
Canada	<u>7.6</u>	4.9	<u>-2.0</u>	3.1
Japan	12.7	12.8	<u>-1.0</u>	2.1
Emerging*	<u>12.6</u>	9.4	<u>3.0</u>	0.8
EM Asia*	<u>13.6</u>	8.6	<u>5.5</u>	0.6
China	14.9	8.9	6.0	-1.0
Korea	4.4	7.0	<u>3.0</u>	7.9
Taiwan	5.8	5.7	<u>4.0</u>	8.9
Singapore	15.9	5.7	<u>1.0</u>	13.0
Latam*	<u>15.9</u>	14.2	<u>-3.6</u>	0.7
Brazil	<u>10.0</u>	11.5	<u>-5.0</u>	-5.2
Mexico	13.7	12.3	<u>-2.1</u>	4.5
Argentina	<u>20.0</u>	9.6	<u>0.0</u>	8.7
Chile	<u>27.7</u>	22.8	<u>2.0</u>	9.9
Colombia	26.5	22.9	<u>-2.0</u>	4.6
Peru	38.1	31.4	<u>-16.0</u>	-6.4
EMEA EM*	<u>5.1</u>	7.7	<u>-0.5</u>	2.0
Poland	-2.8	9.1	<u>-0.9</u>	2.2
Hungary	4.5	3.3	<u>-2.5</u>	3.3
Czech Rep.	1.2	4.2	<u>1.5</u>	-1.8
Romania	22.9	15.2	<u>-2.5</u>	2.4
Russia	<u>2.2</u>	2.9	<u>2.0</u>	0.8
Turkey	<u>10.0</u>	11.5	<u>-4.7</u>	4.0
South Africa	<u>12.0</u>	20.0	<u>-1.5</u>	4.8

* Aggregates are GDP weighted averages of constituents. Source: J.P. Morgan. Any long-form nomenclature for references to China; Hong Kong; and Taiwan within this research material is Mainland China; Hong Kong SAR (China); and Taiwan (China).

Figure 3: Risk bias, 1Q21

%-pts. Nowcast minus forecast



This week we updated our February G4 flash PMIs and December global retail sales (Table 2). In another sign of economic resilience in 1Q, the DM all-industry PMI rose 0.6pt to a two-year high of 53.0 in February. Global retail sales weakened for a second consecutive month in December. However,

the US has already reported a dramatic January rebound. We also updated G4 household income and consumption through 4Q20 and summarized recent revisions to the growth outlook. In the G4, the saving rate ended last year roughly 7%-pts above its pre-pandemic level—pointing to ample fuel for consumer spending ahead. Our forecast for global GDP growth in the five quarters starting from 4Q20 has risen 1.6%-pts since November, owing to stronger 4Q performance in Europe and an improved fiscal outlook for the US.

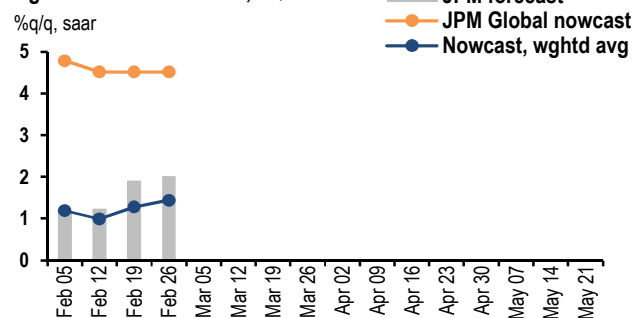
Table 2: J.P. Morgan global aggregates

%ch, sa (ar for qrt). PMIs are levels. Confidence is st.dev from 2010-pres avg

	4Q20	1Q21	Dec20	Jan21	Feb21	Mar21
PMI, mfg	54.8	54.2	54.9	54.0	54.3	54.4
PMI, serv	52.3	52.3	51.8	51.6	52.3	52.9
IP	15.0	11.6	0.4	<u>1.1</u>	1.0	1.0
Retail sales	4.1	3.1	-0.6	<u>1.1</u>	0.4	0.6
Auto sales	10.1	-8.6	4.2	<u>-5.9</u>	2.3	0.0
G-3 cap. ship.	25.5	9.3	-0.4	<u>1.5</u>	0.6	0.9
G-3 cap. orders	29.5	14.4	1.4	<u>1.1</u>	1.1	1.0
Cap. imports	35.2	26.9	1.5	<u>1.7</u>	1.5	1.5
Bus conf	0.1	0.2	0.2	0.2	<u>0.2</u>	0.2
Cons conf	-0.4	-0.5	-0.4	-0.5	<u>-0.5</u>	-0.4
Nowcast (ar)	5.3	4.5	4.7	4.4	4.3	4.2

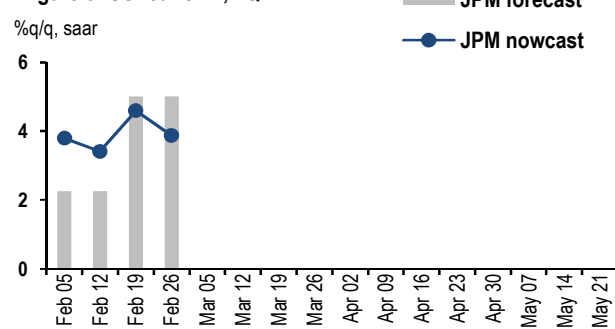
Note. Shaded values show forecasts computed by the Kalman filter estimates from the dynamic factor model. Underlined values are our estimates based on available data and our judgment. Source: J.P. Morgan, Markit, and national statistical agencies.

Figure 4: Global real GDP, 1Q21



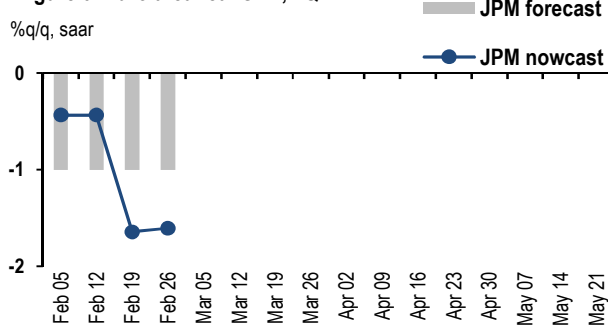
Source: J.P. Morgan

Figure 5: US real GDP, 1Q21



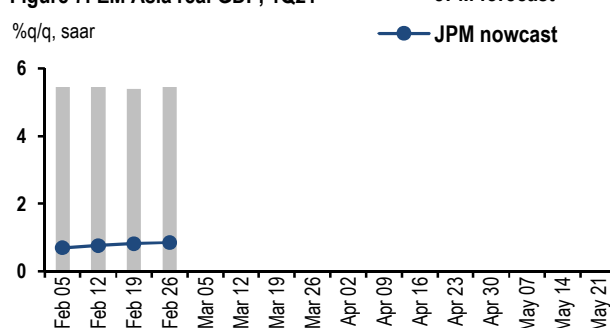
Source: J.P. Morgan

Figure 6: Euro area real GDP, 1Q21



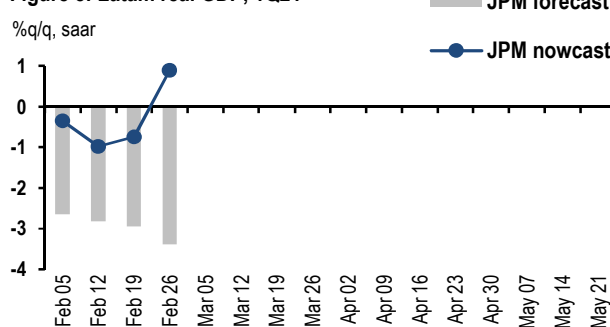
Source: J.P. Morgan

Figure 7: EM Asia real GDP, 1Q21



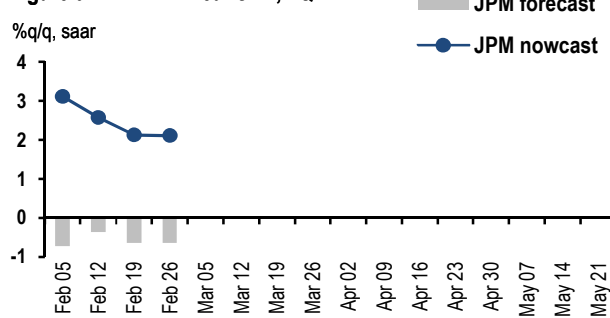
Source: J.P. Morgan

Figure 8: Latam real GDP, 1Q21



Source: J.P. Morgan

Figure 9: EMEA EM real GDP, 1Q21



Source: J.P. Morgan

* For primer on various Nowcasters, click here: [Global](#), [US](#), [EMU](#), [UK](#), [Japan](#), [EM](#).

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The J.P. Morgan View

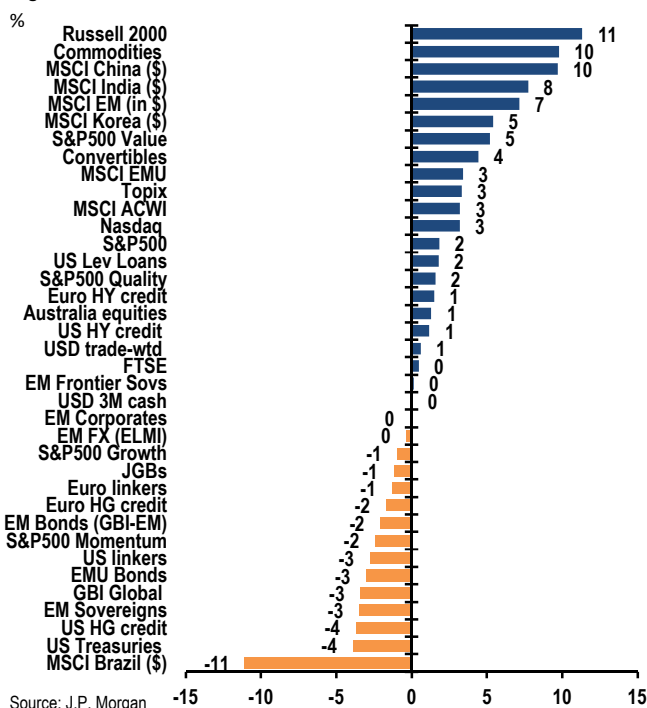
The beginning of the end of easy money is starting to look overpriced

- **Cross-asset strategy:** Higher rates was one of late 2020's most-consensus views, but higher rate volatility was not. Hence, this week's broad deleveraging across Equities, the EM complex and parts of Commodities as the DM Bond sell-off became disorderly. US money markets have been too quick to price the beginning of the end of easy money, which is one reason to think that either the Treasury sell-off eases or the rate rise returns to being a low-vol process. Either would be bullish for risky markets. But don't mistake cheapness in some parts of rates markets with evidence of value and investor underweights across the risky market spectrum. There are still multiple signs of complacency. But it's too soon in the growth, policy and inflation cycles to be defensive. We're now mainly taking risk across and within Equities hedged with Commodities rather than in the EM complex, despite a very punchy view on global growth.
- **New trades:** Moved underweight EM local duration and neutral EM FX ([Goulden](#)); bought 1Y1Y breakevens in Euros and 1Y in Australia ([Diamond](#)); downgraded US HY Energy Credit from OW to neutral ([Hamid](#)); bought 5Y US Bonds ([Barry](#)); bought VIX April puts, April call spreads on XLE and call spreads on commodity-linked stocks ([Kaplan](#)); bought custom basket to hedge against continuous rise in rates ([Silvestrini](#)); recommended dual digital on FTSE100 up/GBP up ([Ravagli](#)).
- **Must-read reports:** [EM vulnerability to a Fed taper](#) (Goulden); [Secular stagnation and the social cost of carbon](#) (Younger); [Explaining the fall in global COVID-19 infections](#) (Mackie); [EMEA Hydrogen: A revolution in need of realism; separating opportunity from optimism](#) (Jones).
- **Economics:** The sharp rise in global bond yields more ratifies our extremely bullish view on growth than it warrants a policy response. We expect the Fed to look past current market volatility and to reiterate that it still is not thinking about (thinking about) rate adjustments or tapering. This does not exclude the potential for a technical 5bp adjustment upward in the IOER in March to stem downward pressure on the Fed funds rate. The ECB's PEPP program allows flexibility in asset purchases to counter any undesired tightening of financial conditions, though we don't expect an imminent response.

- **Equities:** VIX is in a bubble given its disconnect to realized vol ([Kolanovic](#)). Reduce beta of MSCI EM overweight by downgrading Brazil ([Martins](#)).
- **Bonds:** The selloff in Bond yields has roots in fundamentals, but valuations look mispriced. Add longs in 5Y USTs ([Barry](#)) and 5Y Germany.
- **Credit:** We expect \$284bn of HY debt will be upgraded to HG by the end of 2022 while \$38bn of HG will fall to HY this year. ([Beinstein](#))
- **Currencies:** Moved from OW to MW in EM FX ([Goulden](#)). Add GBP shorts. Stay short AUD/NZ, short EUR/USD and long NOK but via options.
- **Commodities:** Brent should rise to 71\$/bbl in Dec 21. Prompt prices are a bit high vs fundamentals. The call is for a time out on the rally ([Kaneva](#)).
- **Catalysts next week:** Earnings & Fed speak (all week); manufacturing PMIs (Mar 1st); Euro area CPI (Mar 2nd); services PMIs, RBA & NBP (Mar 3rd); Euro area retail sales/unemployment, OPEC & BNM (Mar 4th); US payrolls (Mar 5th).
- **JPM View video** (Normand, Barry, Goulden, Martins): [click here to watch](#).

This excerpt of The J.P. Morgan View has been adapted for Global Data Watch.

Figure 1: Year-to-date returns



This year's low-volatility bear market in Fixed Income has morphed into something much more disorderly this week ([chart 2](#)) despite [dovish Fed commentary](#), in turn driving decent drawdown across many of this year's strongest-performing markets. From their February peaks, the S&P500 is only down 3% but the Nasdaq and EM Asia are off 7%. Volatility is higher across the board, but as both implied vols and volatility risk premia have been above average all year in Equities and Credit, the rally in vols has been modest.

The greater corrections are coming in markets synonymous with the typical speculative excesses of an easy-money era ([chart 3](#)). A few examples include: US IPO stocks that had delivered record outperformance versus the overall S&P500 this year, but are now down 15% from peak; the ARK Innovation ETF, down 20% from peak; or cryptocurrencies, down 22% from peak. For the traditionalists who still earn their crust through traditional indices – maybe out of a simple need for liquidity rather than denial of the future – a multi-asset portfolio of Equities and FICC is up about 1.5% year-to-date, so in line with its average. From that perspective, this week's correction has realigned the pace of returns with trend rather than imposed some extraordinary loss.

Shouldn't everyone have seen this coming? They did – directionally but not in vol terms. In December when we marketed year-ahead outlooks to Zoom screens checkered with black boxes of those bored by consensus views, it was obvious that investors were bearish on Bonds, bullish on Equities, bearish on the dollar, bullish on the EM complex and skeptical about the duration of Value rotation. Our confidence in still advancing these recommendations was based on two observations: that there was a gap between views about reflation and position for all aspects of it; and that the consensus baseline itself could improve over time due to policy changes like US fiscal decisions ([chart 4](#)).

While we shared the bearish view on DM rates, we thought the adjustment higher would be low-to-moderate vol even in the face of very strong growth and firmer inflation. Vol shocks occur when regime shifts meet overvalued, over-owned markets. The end of easy money will be a regime shift, but in our view, it would be a protracted, multi-phase one involving a tapering announcement (late 2021); an extended implementation (2022, over perhaps more months than the Fed's 10-month execution in 2014); and a pause before a first hike (sometime in H1 2024).

We have been very comfortable positioning the portfolio in exposures that would benefit from reflation with or without a tapering (curve steepeners, OW breakevens, OW Equities vs Bonds & Cash, OW Value vs Growth, OW non-

US vs US Equities, OW Commodities ex Gold), but we didn't want to recommend exposure that might require a multi-week, high-vol pricing of bond yields (long USD vs EM FX, UW EM Equities). The risk was always that the feared event became self-fulfilling on minor catalysts (like short-term upside surprises on US inflation as the economy boomed), given that by late January many markets looked richer in valuation and more over-owned in terms of positioning than in spring 2013 (see [Could the Fed taper without a tantrum? Unlikely given current valuations and positioning](#) in the Jan 22nd *J.P. Morgan View*).

Now that risk has become reality, the big call to make is whether this move is barely or mostly complete. We're biased towards the later, based largely on valuations, a bit on positions and a bit on policy. Before this week's yield spike, JPM's weekly client survey was already signaling reasonably widespread duration shorts. Also, a basic fair value model relating DM bond yields to cyclical and policy drivers like growth momentum, policy rate expectations and central bank balance sheet growth was already signaling that yields were about 20bp too high ([chart 5](#)). Hence, why rate forecasts have been bearish, but tactical strategy has been neutral.

Front-end valuations have become much more challenging for those expecting more deleveraging, considering how the Fed might operate under average inflation targeting. OIS rates now price a first Fed hike by spring 2023, and about four hikes by end 2024. That timing and speed of liftoff should seem aggressive to anyone who thinks that the US economy must reach full employment to see core inflation near 2%; then need to operate above full employment for some time to generate a mild, inflation overshoot; then need to maintain +2% core for perhaps a year to justify a first hike. If the first hike might not come until three years from now, then the recent movement in 2023 and 2024 OIS rates is starting to look as overdone as the reaction in 2015 contracts when the tantrum occurred in 2013 ([chart 6](#)). Hence why our US Treasury strategists now recommend buying US 5Y notes (see [US Treasury Daily: Making a fire](#) by Barry from Feb 25th). The view doesn't rest on Fed intervention, particularly when the tightening of overall financial conditions this week has been small.

If rates stabilize soon on value considerations or if they rise but in a low-vol manner, we are fairly sure that Equities will revive, spreads grind tighter and some EM currencies appreciate (higher-yielders like MXN, cheap ones like RUB, those with strong current account surpluses like CNY and KRW). This rally will not be because risky markets are cheap or under-owned. Indeed, the message from our **cross-asset complacency indicator** launched a few weeks ago is that vulnerability remains near a 20Y high due to expensive val-

uations on any measure and investor positioning on some measures (see [Complacency and fear indicators for multi-asset portfolios](#) by Normand & Manicardi from February 11, 2021). The reason for gains are that strong growth momentum and loose monetary policy tend to drive risk-taking, even if that means expensive markets become more expensive. In a more conservative case, risky markets could still beat cash and Bonds by growing into high valuations, meaning that Equities could rise with earning growth but not re-rate, and Credit could earn just its carry.

If we're wrong on the baseline for a low-to-moderate vol bear market in Bonds, it will probably be because the US more quickly attains 2% core inflation, thus shortening the gap between Fed tapering and tightening even if the Fed still takes a year to wind-down asset purchases. Note that the US curve is not steep relative to even the current level of breakevens, much less a higher inflation outcome ([chart 8](#)). And yes this risk is most directly hedged with TIPS, but it is most profitably hedged with Commodities that rise more hyperbolically when output gaps close, inventories draw and strong demand meets short-term, inelastic supply. Oil markets look far from tight based on how inventories are relative to their typical post-recession levels ([chart 9](#)), but this is also the commodity with more scope to profit from demand normalization as vaccines restore international air travel and domestic commuting. Some Base Metals have less of a demand surge to look forward to if China is slowly tightening credit growth, but inventories are much leaner than typically holds after a recession ([chart 10](#)).

Whatever sector one chooses, remember this: portfolios aren't unhedgeable when rates are low, if the next macro shock could be too much inflation rather than too little growth. When inflation is high enough to threaten margins or the easy money environment as in the 1970s and early 1980s, the Equity/Commodity correlation can turn negative and thus replace the insurance value that traditionally came from a negative Equity/Bond correlation ([chart 11](#)). There will be a time when Commodities like Oil and Base are too expensive and too over-owned to serve this function, in which case rotation into unloved Gold will make sense (see [Some like it hot: the best and worst inflation hedges as the US goes big on fiscal stimulus](#) from the Feb 19th J.P. Morgan View). But that time isn't now.

Equities

Global equity markets were weaker into the end of the week, due to worries over the too fast repricing of bond yields, and a move up in real yields. Value was strong vs Momentum. Travel & Leisure, Banks, Energy and Insurance were the best performers this week, while Tech and Staples

were the worst. Regionally, European equities outperformed, while Asia lagged.

Our Global Equity strategists were looking for a breakout in bond yields, and expect further repricing. They believe that equities should be able to absorb well the current breakout. Value rotation should advance in this backdrop, as long as yields are rising for the right reasons – growth backdrop remains supportive and tapering concerns are pushed out. They address UK outlook, where consensus is increasingly bullish. In their view, while the risk-reward for the region has improved, it still does not warrant an OW stance. On the positive side, apart from the very weak performance, where UK lagged both the US and Eurozone for 5 years in a row through 2020, valuations are cheap, dividends are coming back, Brexit is to some extent behind us and the UK is a play on COVID recovery, as it was disproportionately hit by the virus. Having said that, the end result might be more robust GBP and higher UK yields, which could offset the benefits for stocks. UK consumer re-opening names form a very small part of the index. UK has one of the most negative correlations to bond yields direction, both short and long term. What is more, UK tended to underperform during every single Value rally seen in the past 10 years. UK shows an inverse correlation to GBP, it has below 1 beta to global equities, as well as to PMIs. Within UK, domestic stocks and consumer reopening plays could do well and the strategists remain OW FTSE250 vs FTSE100. On the other side, Miners could start fading as the China credit impulse, a clear lead indicator, has peaked, and the last 4 quarters worth of a tailwind from weakening USD might not repeat (See [Equity Strategy](#) and [Equity Strategy](#) by Matejka et al from Feb 22nd and 15th). On Q4 earnings, delivery has been much stronger vs consensus with surprises running at 18% in Europe and 10% in the US. At a sector level, Energy and Industrials have done poorly, while Tech has fared better (See [Q4 Earnings Season Tracker](#) by Matejka et al from Feb 26th).

Our quantitative and derivatives strategists note that, while there is a lot of talk about bubbles – it is hard to see one in the broad equity market. In their view, there is one asset that is currently in a bubble – the VIX. The VIX is now disconnected to underlying short term S&P 500 realized volatility, indicating a bubble of fear and demand from investors looking to hedge or profit from a hypothetical market selloff. (see [Market and Volatility Commentary](#) by Kolanovic et al from Feb 24th).

Our EM strategists reduced the beta of their EM model portfolio. We could be at a transition point where positive news continues to come, but the slope of improvement declines. That would be consistent with EM equities entering a period of consolidation before breaking higher their base-bull

range of 1,450 to 1,600 for MSCI EM (see [Less Beta: More alpha](#) by Martins et al from Feb 25th).

Bonds

Bonds sold off this week as optimism over the recovery and the reflation trade snowballed into a more disorderly position unwind. In the US, the bearish steepening for much of 2021 has roots in fundamentals given expectations of an additional of \$1.7tr of fiscal stimulus and a return to more normal mobility later this year. However, this week's moves have seen market pricing of eventual Fed hikes that seem out of line with fundamentals. In addition, a decline in market depth likely contributed to the outsized moves in yields. Our strategists see Treasury yields at current levels as somewhat mispriced and entered tactical longs in 5Y USTs (see [UST Market Daily](#) by Barry et al from Feb 25th).

In the **Euro area**, our strategists see the sell-off pricing in a very rosy macro scenario given the weaker starting point on inflation and relatively slower recovery pace, and expect the ECB to step up its rhetoric and recalibrate PEPP purchases to stabilize intra-EMU markets in case of any further uptick in vol or tightening in financial conditions. They add tactical longs in 5Y Germany as the sector looks cheap even after adjusting for excessive money market tightening. Intra-EMU, they stay long 10Y Italy vs. Germany and hold 10s/30s Italy flatteners.

In the **UK**, our strategists expect the sell-off in 10Y gilts to run out of steam with current levels marginally above 2Q21 targets and remove their bearish duration bias. They take profit on 1Yx1Y/5Yx5Y GBP swap curve steepeners, and tactically receive 1Yx1Y SONIA as front-end valuations look cheap. In **Australia**, in response to indiscriminate selling on the front-end of the AUD curve, our strategists expect the RBA to take more forceful action within its YCC commitment. They add longs in 2Yx1Y AUD swaps and stay long 10Y ACGBs vs. USTs. In **Japan**, the focus in the near-term is likely on how the BoJ will react to upward pressure on 10y JGB yields. Our strategists keep 30s/40s JGB curve steepeners.

In **EM**, the rise in US 10-year real yields has been brought forward by the expectation of a larger US fiscal stimulus as well as better-than-expected data. While the global reflation outlook also has some positive implications from higher growth expectations, higher US real yields typically imply tighter financial conditions and tend to weigh on EM. Going into 2Q, global growth leadership shifts to the US adding some headwinds (see [EM Strategy Update](#) by Goulden et al from Feb 24th). Our EM strategists are now UW local duration. In EMEA, they are UW Poland and Czech vs. OW Russia (see [EMEA EM Local Market Compass](#) by Siddiqui et al

from Feb 26th). In Asia they are OW China and Indonesia vs. UW Malaysia. In Latam, they are UW Chile and Peru vs. OW Mexico.

Credit

The rise in bond yields and decline in stocks over the past week seems to have passed the credit market by! Spreads have moved broadly sideways. This, of course, raises the usual question. Are spreads projecting a false sense of security to creditors given their natural tendency to lag moves in other risk markets? Possibly, though our strategists think creditors need to make a choice between what version of reflation they believe in; an accelerated, yet orderly version where spreads move tighter; or a disorderly version in which policymakers are seen to lose control of the narrative, bond yields gap higher still and spreads widen as volatility rises. The base-case scenario remains one of accelerated, yet orderly reflation and tighter spreads.

Our North America HG and HY strategists collectively expect \$284bn of HY debt to be upgraded to HG by the end of 2022 and forecast \$38bn of HG debt to fall to HY this year (see [Rising starts to outshine fallen angels](#) by Beinstein et al from Feb 24th). This is about 11% of the debt currently rated BBB- with a negative outlook. In an environment where there continues to be demand for loans relative to HY bonds (2021 CLO issuance forecast was recently revised to \$105-115bn from \$85-95bn) these dynamics support the case for further compression.

Currencies

The re-pricing of US and global monetary policy and the concomitant slippage in break-evens has destabilized risk sentiment and high-beta currencies this week - i.e. the rise in real yields is starting to outpace the rise in nominal yields, a hallmark of the taper tantrum in 2013. Our strategists have been flagging the risk of a bond-yield backup in 2021 since late last year, and more recently have flagged how this could shift correlation regimes for FX. The regime shift occurred with a vengeance this week and in this week's [FXMW](#) they assess in more detail the issue of yield-thresholds by individual currency blocs. They also consider the relevance of the bond-equity correlation for FX, as well as the increased relevance of yield differentials as a driver of currency returns.

The near term risk is for a continued reassessment of central bank policy, and an associated de-risking of investor positioning. Well-positioned reflation trades in FX thus remain vulnerable, albeit commodity-FX can still fall back on elevated terms of trade support so the rug has not been pulled from underneath them entirely. Further out, the primary risk is for a more pronounced, USD-supportive rise in UST yields

vs other DM markets given that the US is delivering uniquely large fiscal stimulus. Wider cross-market spreads in favour of USD should thus be a continued feature of the year as the US leads the recovery in GDP back to pre-pandemic levels and beyond.

This translates into both tactical and strategic risks against high-beta currencies. They already have been trimming risk in the portfolio over recent weeks, in addition to reducing USD shorts, while our EM colleagues cut their EM FX OW recommendation earlier this week (see [Stepping aside in Local Markets](#) by Goulden et al from Feb 24th). Thus, no change is made to the existing suite of selected high beta longs, and instead GBP is sold given its recent outperformance against rates and its relatively-elevated positioning. They still hold longs in EM FX with solid structural supports (CNH) and constructive fundamentals and valuations (RUB), while last week they optionalized G10 oil exposure (NOK) to limit downside in the case of choppy market conditions. They also hold short AUD/NZD and short EUR/USD.

Commodities

Brent prices closed Wednesday at \$67/bbl—the highest level in more than a year as the market looks ahead toward an accelerated decline in record inventories. A lot of things are moving in oil's favor. On the supply side, OPEC+ discipline and Saudi Arabia's decision to reduce output by 1 mbd through March were further amplified last week when US crude production fell 3.2 mbd amid an unprecedented polar blast. From the demand perspective, the winter of 2021 stands out as one of the coldest in decades, upending energy markets and sending prices for electricity, fuel and vessels to record highs. According to Platts, extreme winter weather over January and February added 1.3 mbd and 0.8 mbd, respectively, to each month's oil consumption in the US, Europe and Japan alone, compared to year ago levels.

Reflective of this tightening, our strategists slightly boost their 2021 Brent oil price forecast by \$3/bbl, while keeping 4Q21 forecast unchanged at \$68/bbl (\$71/bbl December average). They also lift the 2022 average price forecast by \$6 to \$72/bbl, fully aligning price forecasts with their model-predicted values. Their price deck is now 2% above the futures curve for calendar year 2021 and 21% above calendar year 2022, with 2Q22 at a 27% premium to the futures curve. Having said that, prompt futures prices seem to be a bit high vs. fundamentals at the moment, likely driven by significant improvement in sentiment which is not captured by their model. This exuberance is evident in the price momentum signal, which remains in extreme territory, suggesting a risk of profit-taking or mean reversion signals being triggered. The acknowledgment of this froth drives the decision not to raise 2021 price forecasts beyond the \$3 implied by the faster

inventory normalization. In other words, the call is for a time out on the rally for the time being (See [Oil Markets Weekly](#) by Kaneva et al from Feb 25th).

Cross-asset forecasts & strategy

Rates	Current	Mar-21	Jun-21	Sep-21	Dec-21
US (Fed funds)	0.07	0.00	0.00	0.00	0.00
10-year yields	1.49	1.35	1.50	1.60	1.65
Euro area (depo)	-0.50	-0.50	-0.50	-0.50	-0.50
10-year yields	-0.26	-0.40	-0.35	-0.25	-0.20
Italy - Germany 10Y (bp)	102	90	80	75	90
Spain-Germany 10Y (bp)	68	60	55	50	55
United Kingdom (repo)	0.10	0.10	0.10	0.10	0.10
10-year yields	0.82	0.70	0.75	0.85	1.00
Japan (call rate)	-0.10	-0.10	-0.10	-0.10	-0.10
10-year yields	0.15	0.10	0.10	0.15	0.15
EM Local (GBI-EM yield)	4.66		4.20		4.29
Currencies	Current	Mar-21	Jun-21	Sep-21	Dec-21
JPM USD Index	119	117	116	116	116
EUR/USD	1.21	1.20	1.20	1.19	1.18
USD/JPY	107	102	101	99	98
GBP/USD	1.39	1.37	1.36	1.35	1.34
AUD/USD	0.77	0.76	0.74	0.72	0.71
USD/CNY	6.48	6.35	6.25	6.25	6.25
USD/KRW	1123	1090	1070	1050	1050
USD/MXN	20.91	19.50	19.50	19.75	20.00
USD/BRL	5.57	5.30	5.20	5.30	5.40
USD/TRY	7.42	7.20	7.30	7.50	7.65
USD/ZAR	15.15	15.00	15.50	15.75	16.00
Commodities	Current	Mar-21	Jun-21	Sep-21	Dec-21
Brent (\$/bbl, qtr end)	66	62	65	66	71
WTI (\$/bbl, qtr end)	62	59	62	63	68
Gold (\$/oz, qtr avg)	1,720	1,815	1,790	1,720	1,650
Copper (\$/ton, qtr avg)	9,428	7,700	7,000	6,800	6,500
Aluminum (\$/ton, qtr avg)	2,214	2,070	1,900	1,800	1,740
Iron ore (US\$/dt, qtr avg)	172	155	135	125	120
Wheat (\$/bu, qtr avg)	6.6	6.2	6.1	6.0	6.3
Soybeans (\$/bu, qtr avg)	14.0	10.7	10.5	10.5	10.5

Source: Bloomberg, Datastream, J. P. Morgan

Credit		Current	Dec-21
US High Grade (bp over UST)	JPM JULI	121	110
Euro High Grade (bp over Bunds)	iBoxx HG	96	90
US High Yield (bp vs. UST)	JPM HY	419	425
US Lev Loans (bp vs. 3Y Index)	JPM LL	430	450
Euro High Yield (bp over Bunds)	iBoxx HY	313	300
EM Sovereigns (bp vs. UST)	JPM EMBIGD	354	325
EM Corporates (bp vs. UST)	JPM CEMBI	235	225
Equities		Current	Dec-21
S&P 500		3,838	4,400
MSCI Europe		1,659	1,830
MSCI Eurozone		236	268
FTSE 100		6,483	7,100
Topix		1,864	1,900
MSCI EM (\$)		1,384	1,450
MSCI China		119	125
MSCI Korea		996	900
MSCI Taiwan		653	605
MSCI India		1,709	1,430
Brazil (Ibovespa)		111,113	134,000
Mexico (MEXBOL)		44,560	46,300
MSCI South Africa		1,501	1,795

Equity sector recommendations & year-to-date returns

	US	Europe	Japan	EM
Energy	29% OW	17% N	30% N	5% N
Materials	2% N	9% OW	6% N	9% OW
Industrials	2% N	4% N	10% OW	5% N
Discretionary	-2% OW	4% N	8% OW	7% OW
Staples	-5% UW	-5% UW	-1% N	-2% UW
Healthcare	0% OW	-2% N	-5% UW	0% UW
Financials	11% OW	10% OW	15% OW	3% OW
Technology	0% OW	6% N	6% N	12% N
Comm Services	5% N	3% UW	14% UW	17% N
Utilities	-5% UW	-5% OW	3% UW	0% UW
Real Estate	4% UW	-5% UW	14% N	6% OW

Core strategic and tactical recommendations by asset class

	Strategic (6M to 2Y trades)	Tactical (1M to 6M trades)
Asset allocation	Above-average OW of DM Equities & HY Credit vs Cash/Bonds; small OW of EM complex – Equities, Sovereigns & Corporates but short duration and neutral FX	No major changes in February edition of Global Asset Allocation
Equities	Country: biased towards US after Value rotation is more complete Sector: OW Healthcare; UW Staples, Utilities, REITs Style: biased towards OW Growth again	Country: OW EM ex China, EMU & Japan vs US, UK, rest of world Sector: OW Cyclical (Discretionary, Financials, Energy) Style: OW Value
Bonds	DM Duration: Neutral EM Duration: OW China, Russia, Indonesia, Mexico, & UW Chile, Peru, Czech, Poland, Malaysia in GBI-EM.	DM Duration: long US (5Y) and Germany (5Y) DM Curve: neutral DM Inflation: long in US (5Y5Y), Euros (1Y1Y) & AU (1Y) DM Spread: OW Spain (10Y) vs GE; OW AU (10Y) vs US US HY: OW CCCs & Bs vs BBs
Credit	US HG: OW Yankee Banks, Energy, Utilities, Cap Goods & Telecoms; UW US Banks, Healthcare, Tech & Retail US HY: OW Gaming, Transport; UW Healthcare, Tech, Cable, Paper, Industrials Euro HG: OW Autos, Toll Roads & Mail, Transport; UW Healthcare, Chemicals, Tech, Media Euro HY: OW Transport, Paper, Retail; UW Chemicals, Telecoms	Euro HG: Long AT1, sold protection on Itraxx Main super senior Euro HY: Long Itraxx Crossover vs Sub Financials EM Sovereigns: OW Pemex, Nigeria, Egypt EM Corporates: favour HY over HG globally; OW China (Property), CEEMEA Utilities, Latam Commodities
Currencies	Few strategic trades; most currency positions are tactical	Short EUR vs RUB, USD & JPY; long CNH & TRY vs USD; OW RUB, MXN, CNY, IDR & CZK vs HUF, CLP in GBI-EM
Commodities	Long JPMCCI Agricultural sub-index	Long Oil, short Gold & neutral Base Metals

Source: J.P. Morgan flagship weekly and monthly strategy publications, including [Global Asset Allocation](#), available on www.jpmm.com. Red shading indicates higher-conviction view

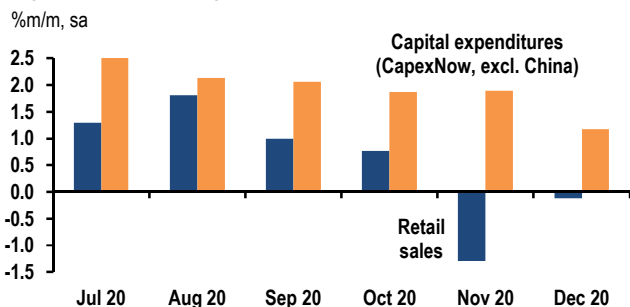
Economic Research Note

Global capex immune to the second wave

- **Capex recovery uninterrupted by second COVID-19 wave, outpaced consumer goods as of December**
- **Strong profit bounce-back, boomy credit, and exuberant animal spirits underlie the recovery**
- **Employment spending still takes back seat to capex**
- **In a post-COVID-19 work-from-home world, tech capex surges while structures languishes**

Global business equipment spending (capex) has fared remarkably better than feared since the start of the global pandemic, and the latest developments point to a continued strong recovery through 2021. In contrast to the recoveries from the past two recessions, global capex nearly recovered its pre-recession level within just two quarters. In addition to rebounding more quickly and forcefully than initially expected, business capex has weathered the second wave of the pandemic better than consumer goods spending. Indeed, as the second wave built through 4Q20, consumer goods spending slumped 0.7%/m on average over November and December (Figure 1). By contrast, most indicators of capital goods activity continued to boom. Our filtering of these data through our global capex nowcaster ([CapexNow](#)) suggests global (ex. China) business equipment spending continued to expand at a boomy 1.5%/m pace while consumer spending was downshifting over this period.

Figure 1: Global final goods demand



Source: J.P. Morgan

We attribute the outperformance of global capex to businesses' willingness to look through the second wave-related slow-down in demand to the coming boom in fiscal-policy supported spending as the pandemic fades with mass vaccinations gaining traction by midyear. The resilience of business capex owes in part to the more targeted approaches governments have taken in restricting activity as well as to a less panic-

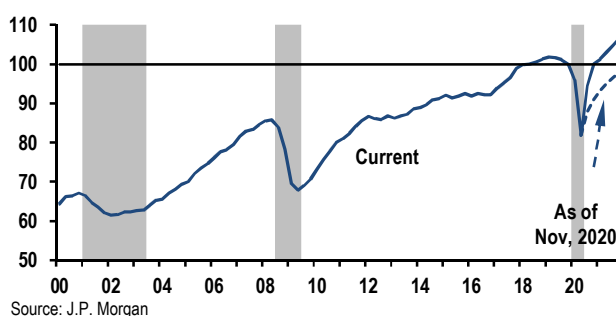
driven response of the private sector compared to last year. Consequently, even though the number of new cases, the rate of hospitalizations, and even the rate of mortalities has been notably higher in the second wave, global real GDP continued to expand at a boomy 8.2% ar pace last quarter and we expect it to continue growing in the current quarter, albeit at a slower 1.9% ar pace. On balance, the resilience of capex through end-2020 is an encouraging sign that the second wave will slow but not derail the recovery. Looking forward, we expect global demand to boom from 2Q through early near year. With a continued strong recovery in profits, we look for global capex to decelerate in 2021 but maintain robust 5%-10% ar growth.

Capex: Fast and steady wins the race

One of the most impressive aspects of the global economy's resilience to the second wave, and indeed of the recovery overall, has been the strong performance of business investment. At the start of the expansion we expected that growth in global capex would be held back by businesses' reluctance to invest with so much uncertainty around the pandemic, weakened profits, levered balance sheets, and limited free cash flow available for investments. Instead, profits have surged back quickly and uncertainties have abated with the rapid discovery of a suite of vaccines.

Figure 2: Global (ex-China) capital expenditures

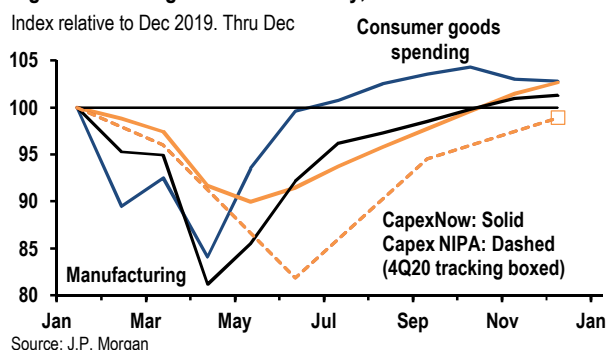
Index, 4Q19=100; fcast 4Q20-4Q21



Source: J.P. Morgan

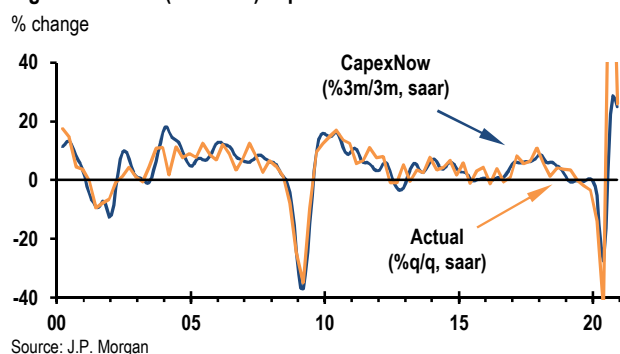
In contrast to our projection just three months ago that global capex (ex. China) would not regain its pre-pandemic level until end-2021, this now looks to have happened a year earlier (Figure 2). Incorporating the latest capital goods-related data, the global CapexNow stood 2.7% above its December 2019 level at the end of last year (Figure 3). While this is running ahead of our tracking of the official NIPA capex data, which stands closer to 1% below its pre-pandemic level, the message of a robust recovery through 2H20 is the same.

Figure 3: Global goods sector activity, 2020



We assess global capex through our CapexNow, which filters all the capital goods data at our disposal, both actual activity and survey-based. The CapexNow is a good tracker of actual capex, even if it did not fully capture the unprecedented slump and rapid recovery in 2020. In this regard, while the CapexNow did not fall as deeply as actual capex, the two have realigned more closely by end-2020 (Figure 4). Thus, we will continue to put considerable weight on the CapexNow in tracking global capex through 2021.

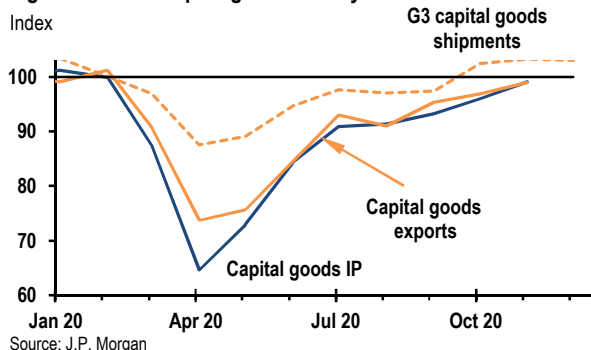
Figure 4: Global (ex-China) capex



Resilience into the new year

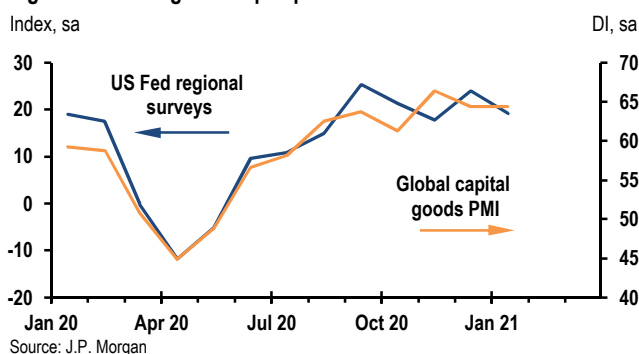
The strong capex recovery has come off the boil in recent months but is still booming even as consumer spending appears to have softened materially around the turn of the year. Global consumer retail sales contracted outright in November and December. By contrast, our monthly global CapexNow, which excludes China for lack of data, marked robust 1%-2% monthly gains from September through December, implying a 25% ar surge last quarter. The strength of global capex is evident across all of our capex-related series, including global capital goods IP, global capital goods exports/imports, and G3 capital goods shipments (Figure 5). Each of these global series now stands above its pre-pandemic level.

Figure 5: Global capital goods activity



Looking to January, the latest survey data point to continued solid gains even as the second wave intensified. In addition to monthly activity data (IP, trade, and shipments), our capex nowcaster also relies on the global capital goods output PMI. After dipping in December to a still solid-level, this index held steady in January. At the same time, the forward-looking component in the global capital goods PMI—the future output index—has moved up in the four months through January. In the US, the regional Fed surveys show a similarly elevated level of capex intentions (Figure 6).

Figure 6: US and global capex plans



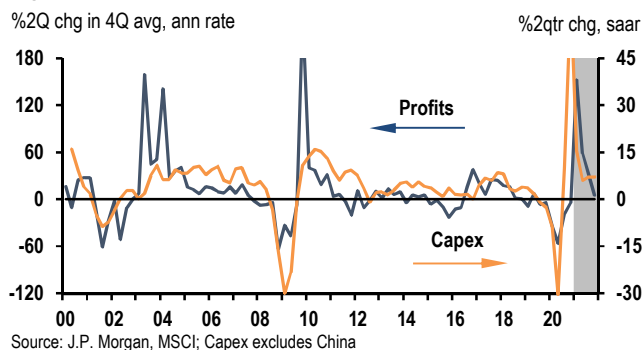
Capex hits the recovery trifecta

Last year's surprising strength in global business equipment spending can be explained through the lens of three fundamental drivers: profits, credit conditions, and business sentiment. After a two-year stretch through the 2018-19 trade war when all three factors stalled and weighed heavily on global capex, these factors bounced back rapidly from the pandemic to support the boom in global capex despite the uncertainties lingering around the second wave:

- **Global corporate profits soared.** Early in the pandemic, we expected global corporate profits to fall 70%oya in 2Q20 and then finish 2021 20% below its pre-pandemic level. Instead, profits fell 36%oya in 2Q20 and we now anticipate the 4-quarter trailing average of global profits to

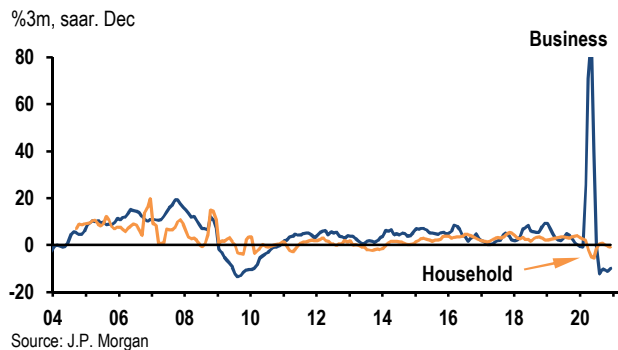
reach above the pre-pandemic level by 3Q21 (Figure 7). However, capex rebounded even faster. The implication is continued solid gains in global capex this year, although not quite as robust having already outpaced the profit recovery.

Figure 7: Global (ex-China) corporate profits and capex



- **Credit booms to businesses.** The faster recovery in capex than witnessed over the prior two recoveries owes in large part to very generous liquidity support to businesses. The macroeconomic landscape in 2020 was remarkable for many reasons, but one of the most astounding developments was the spectacular level of government policy support to businesses. In just three months as the pandemic raged, a flood of fiscal and monetary liquidity boosted bank credit to businesses by 80% annualized, in sharp contrast to the credit crunch that followed the GFC, when credit growth slumped 13% ar in the three months through September 2009. The current episode also differs from the GFC in terms of credit to the household sector, which likely dialed back largely for lack of demand (Figure 8). While credit growth has slowed markedly in the last few months of 2020, credit outstanding remained 9% above its pre-pandemic level in December.

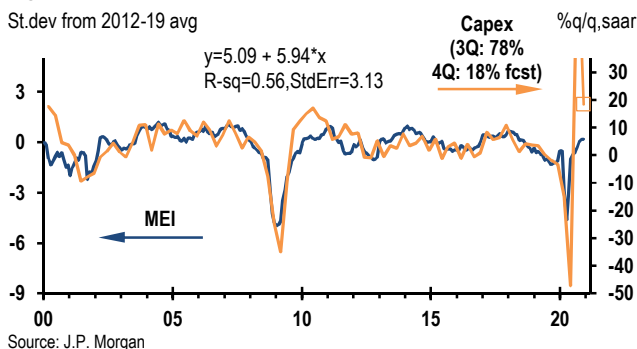
Figure 8: G-4 bank lending



- **Animal spirits look through the pandemic.** In the lead-up to the pandemic, business expectations had been damped by two years of a divisive trade war. After a further collapse in 1H20, business expectations recovered quickly, reaching

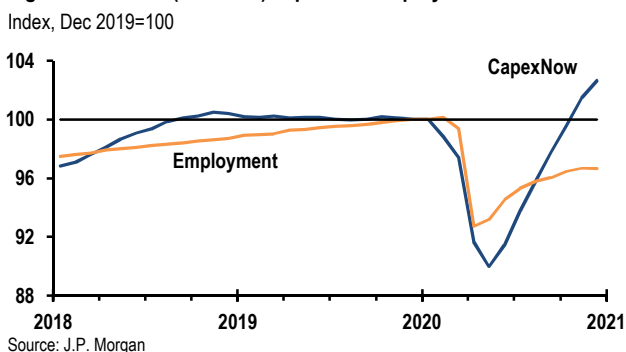
the pre-pandemic level by September and marking a four-year high in December. At its current level, our manufacturing expectations index (MEI) is consistent with strong 7% ar global capex growth (Figure 9). As with credit, manufacturing expectations have more than recovered the pre-pandemic norm even as consumer sentiment is still depressed.

Figure 9: Global capex and MEI



If there is any concern, it is that hiring remains the biggest underperforming aspect of business spending. Despite our CapexNow having reached its pre-pandemic level, global (ex. China) employment remains 4% below its pre-pandemic level. Part of the divergence reflects the significant sectoral divergence between goods and services, with the former far outperforming the latter. However, the service sector comprises a material share of capital investment. As such, the willingness of businesses to invest but not hire shows reticence similar to 2018 as the trade war was heating up (Figure 10). While this is not our call, should the latest stall in global hiring into year-end feed back to weaker consumer spending, business resilience could soon fade.

Figure 10: Global (ex-China) capex and employment



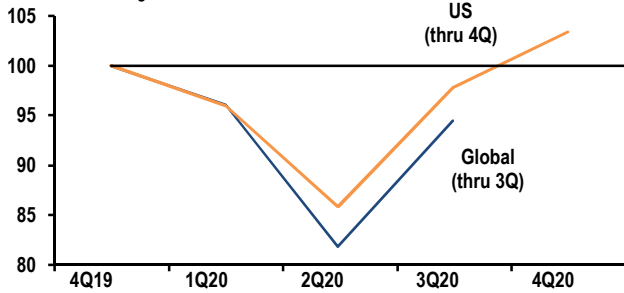
Beneath the recovery surface, IT shines

Overall, the boom in global capex has encompassed most regions and sectors. At the regional level, nearly every economy reported a strong capex bounce in 3Q. Data for 4Q are not yet available for many economies outside of the US. In the US,

capex moved to 3.3% above its pre-pandemic level (Figure 11). Sectoral detail is limited, but the US underscores how the epic surge underway in tech-related spending is translating to capex as well as consumer spending.

Figure 11: Global* business equipment spending

Level. * Excluding China

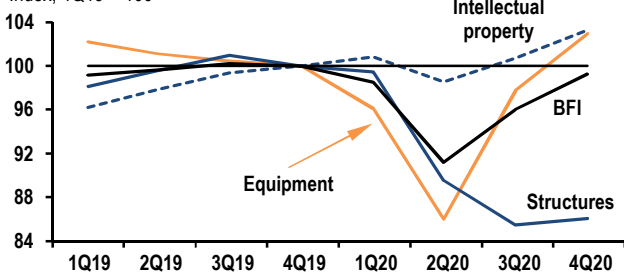


Source: J.P. Morgan

Within the broad “equipment” category of US capex, information processing equipment barely fell during the pandemic and has soared nearly 20% over the past year. Spending on industrial machinery has had a strong recovery after declining in 2Q20, and has regained its pre-pandemic level. Within goods, transportation investment (including aircraft and rental cars) was ground zero for the pandemic hit to growth—slumping over 40% in 2Q20 (not annualized). The segment has seen a boomy recovery but remained over 10% below its pre-pandemic level in 4Q20. The worst-performing sector is non-residential structures (including hotels, malls, and offices), which did not fall as much as transportation investment but has yet to bounce off its low nearly 15% below the pre-pandemic level (Figures 12 and 13).

Figure 12: US private domestic investment

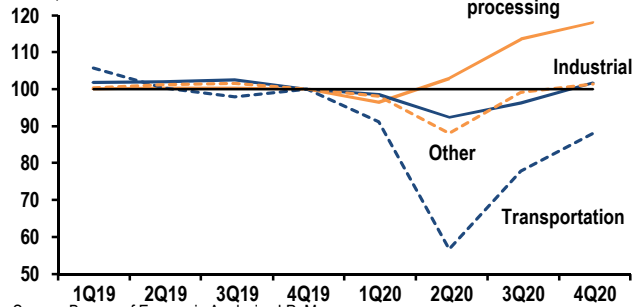
Index, 4Q19 = 100



Source: Bureau of Economic Analysis, J.P. Morgan

Figure 13: US private fixed investment in equipment

Index, 4Q19 = 100



Source: Bureau of Economic Analysis, J.P. Morgan

Economic Research Note

EM fundamentals less vulnerable to a Fed taper

- **The 2013 Fed taper tantrum is burned into EM investors' memories, leading to market focus on EM vulnerabilities ahead of any Fed taper**
- **We do not think that EMs are vulnerable in the same way they were in 2013**
- **Debt ratios are much higher but EM economies do not have the same external imbalances and are not overheated; technicals also look more favorable**

There is renewed focus on how EM will fare when the Fed eventually tapers its asset purchases, given rates are rising and as time progresses we will get closer to a post-pandemic recovery. During last year's market turmoil at the start of the COVID-19 pandemic, the Fed announced another series of large-scale asset purchases (i.e., QE), as part of its response. This QE is an ongoing support to global liquidity and [our economists see the Fed starting to taper](#) its asset purchases toward the end of 2021 given an economic recovery. The 2013 Fed "taper tantrum" started a multi-year trauma for EM assets, with EM local bonds seeing peak-to-trough returns of -33% over three years. This experience is burned into EM investors' memory, leading to market focus already on EM vulnerabilities ahead of the next Fed taper.

EM reliance on foreign capital means it benefits from abundant global liquidity and is vulnerable to changes in liquidity conditions. Asset purchases since March 2020 by DM central banks—and the US Federal Reserve in particular—helped global financial markets recover remarkably quickly from the COVID-19 crash. Risk premia in many assets are now low again. Asset purchases have the effect of displacing capital from fixed income assets that needs to find a home and also lowers yields. The resulting capital searching for higher yields is often drawn to Emerging Markets. A similar environment persisted in the years up to May 2013, with large inflows helping to finance external imbalances of EM countries, prompting currencies to appreciate and local bond yields to fall.

Rising US rates per se are not usually the catalyst for an abrupt EM sell-off, rather rising *real yields* are the risk. The 2013 taper tantrum is the best period to illustrate that the cause of rises in US rates—whether rising breakeven inflation or real yields—matters for EM. We would expect breakeven inflation to rise in an environment of accelerating growth and rising inflation expectations, with commodity prices moving higher. In those environments EM risk assets tend to rally (Table 1). However, rising real yields typically accompany

market perceptions of a tightening shift in US monetary policy and that leads to weaker EM asset prices. What made the 2013 taper tantrum so problematic for EM, using the framework in Table 1, is that real yields rose 175bp and at the same time breakeven inflation fell. The market interpreted it as a tightening of policy and a policy mistake that would curtail growth and inflation. The likelihood of a repeat of that by the Fed is lower but for EM investors deserves particular scrutiny. It is also likely that the environment later in the year when the market actively debates tapering will be one where US growth and inflation are higher, increasing the sensitivity of EM assets to US rates. This may unfold over a long period, as tapering will be only the first part of a period of focus on policy normalization, as it was in 2013.

Table 1: US real rates and breakeven inflation impact on EM fixed income

Return of EM assets to 1% move in 10y US real rates and 10y US breakeven inflation. 10y monthly regression.				
	10y Breakeven	(t-stat)	10y Real	(t-stat)
EMBIG	3.30%	3.5	-5.70%	-7.1
EM FX	5.70%	5.3	-2.30%	-2.5
GBI-EM in USD	4.80%	3.0	-5.80%	-4.3
GBI-EM in LCY	-0.80%	-1.4	-3.40%	-7.4
MSCI EM LCY	13.40%	6.6	-1.50%	-0.9

Source: J.P. Morgan

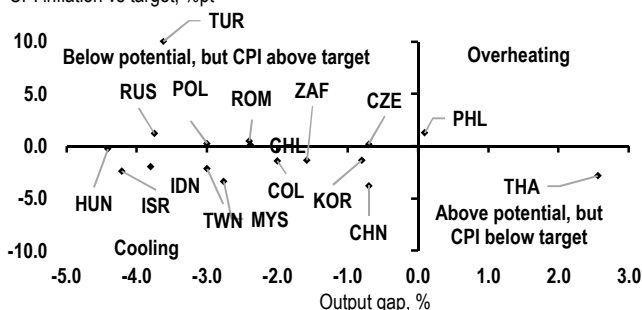
EM vulnerabilities: now versus 2013

The critical difference between economic conditions today and the 2013 taper tantrum is that EM economies are not overheated and largely have no external vulnerabilities, even as fiscal deficits and debt have increased sharply. During the 2013 taper tantrum, the fear in the markets was that EM economies were overheating, fueled by loose macroeconomic policies and expansion of credit to both the private and public sectors. Concerns over growth fundamentals amid large current account deficits led to an adverse market reaction as investors abruptly withdrew capital, triggering a financial crisis.

Economic fundamentals are less conducive to large-scale outflows this time around. Aside from China's remarkable recovery, the rest of EM is still recovering the severe output losses during the pandemic. Even as growth and inflation are rebounding, overheating concerns largely remain absent (Figure 1); the EM ex. China output gap ended 2020 at -3.3%, roughly on par with the GFC trough in 1Q09. However, unlike the post-GFC period when the EM roared back, the current outlook is for slack to persist (-1.9% in 4Q21 and -1% in 4Q22). If we are right, EM core inflation will remain stuck near a two-decade low even as headline inflation rises on the back of higher commodity prices. Consequently, any adjustment to external shocks akin to a taper tantrum is unlikely to involve large policy rate hikes, a big reduction in current account deficits, or a steep growth slowdown, in our view.

Figure 1: EM output gaps and inflation

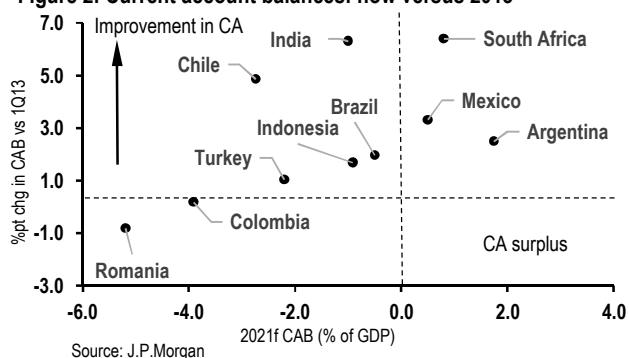
CPI inflation vs target, %pt



Source: J.P. Morgan

During the 2013 taper tantrum, markets focused on countries with persistent current account deficits (CADs) many of which also were running “twin deficits” (fiscal and CADs). External vulnerabilities are much more limited this time around with many of the “Fragile 5” (Brazil, Turkey, South Africa, India, and Indonesia) running broadly balanced current accounts. Figure 2 shows that CADs have narrowed sharply since 2013, and the latest four-quarter rolling CADs of the Fragile 5 are now at just 0.4% of GDP versus 4.4% ahead of the taper tantrum. India, Brazil, and South Africa are in fact running basic balance surpluses, as opposed to large deficits back in 2013. Several EM low-yielders, such as Hungary, the Philippines, Malaysia, Korea, and China, have seen their current account surpluses shrink from taper tantrum levels.

Figure 2: Current account balances: now versus 2013



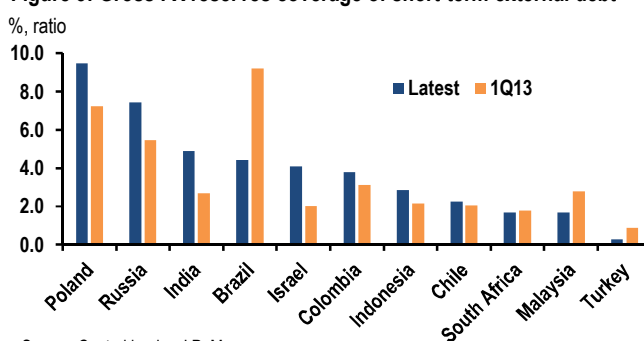
Source: J.P.Morgan

Among the CAD countries, only Romania appears to be in a worse position, having seen its CAD widen from just before the 2013 taper tantrum to 5% of GDP. On a 4-quarter rolling basis, Turkey and Colombia were also running relatively large deficits of 3%-4% of GDP in 2H20. In Turkey’s case, after the huge government-engineered credit stimulus in 1H20, we expect the CAD to narrow sharply this year on the back of policy normalization. Colombia has long run a “structural” CAD above 3% of GDP, and while lower FDI funding is a concern, the BOP has in fact been over-financed after Colombia tapped its IMF FCL. While we expect Romania’s CAD to keep widening, to more than 6% of GDP in 2022, EU funds

and FDI should provide the bulk of the financing with limited reliance on bond inflows as well as provide a sizable buffer that can substitute for external issuance.

Despite smaller CADs, FX reserve adequacy metrics are in some cases weaker than they were at the time of the taper tantrum. FX reserves are frequently discussed in terms of protecting a country from vulnerability as it can be a mechanism to defend against currency pressures and help smooth volatility and avert balance of payments crises. FX reserves relative to short-term external debt are lower in Turkey, Brazil, and Malaysia compared with 2013 (Figure 3). Turkey in particular has seen large-scale FX reserve losses over 2020 to its lowest on record by a wide margin.

Figure 3: Gross FX reserves coverage of short-term external debt



Source: Central banks, J.P. Morgan

Over the past year residents, rather than foreign investors often played a more significant role in determining capital flows. In this case, how much FX reserves cover the domestic money supply also can be a critical indicator of vulnerability especially in the context of rapid expansion of monetary aggregates. A low ratio, typically less than 20%, suggests a lack of protection in case there is domestic capital flight. A handful of countries have sub-optimal FX reserves on this metric, namely, South Africa, Turkey, Argentina, Chile, and China. Several others like Korea, Malaysia, and Indonesia also have too-low ratios, although macro-prudential measures that limit the speed and magnitude of domestic liquidity withdrawal (e.g., limits on how much domestic pension and insurance funds can buy in foreign assets) act as a mitigating factor.

Excess private savings and QE provide insulation

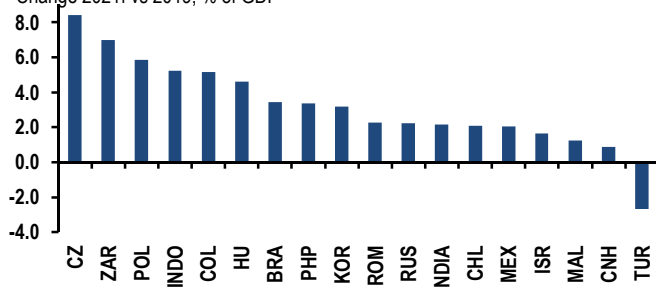
Large increases in EM private sector savings provide insulation against external vulnerabilities this time around. Economic theory links current account deficits with the private saving-investment gap and the fiscal deficit. Without an adjustment in the private saving-investment gap, current account and fiscal deficits must move in tandem, creating a twin deficit. A twin deficit indicates vulnerability as countries with larger deficits require more avenues to fund it, increasing their

reliance on external markets. Despite the projected narrowing in fiscal deficits this year the average EM budget gap will still be 3.5% of GDP larger than at the time of the 2013 taper tantrum (South Africa stands out with a projected 2021 budget gap that is over 7% of GDP higher than it was in 2013). However, private sector net savings also increased substantially in the wake of the pandemic as consumers and businesses treated the economic shock as [a permanent shock to their incomes and earnings](#).

This sharp rise in savings drove a marked improvement in current account balances in addition to limiting the size of EM QE. Importantly, our forecasts suggest that the massive increases in private savings accumulated over 2020 will not be fully unwound this year—we expect EM private sector net savings will still be around 3%-pts of GDP higher in 2021 than before the pandemic (**Error! Reference source not found.** 4), and in some countries like SA that implied increase in net savings will be as much as 6%-7% of GDP. This suggests most EMs, including many of the high-yielders, still have space to fund higher deficits and support growth without straining financial stability. Unless net savings drop below pre-pandemic levels a sustained reflation dynamic also is less likely to play out.

Figure 4: Private sector net savings

Change 2021f vs 2019, % of GDP



Source: J.P. Morgan

Limited and time-bound use of EM “QE” programs helps to further mitigate vulnerabilities relative to 2013. The EM policy response to the 2013 taper tantrum followed the well-established pattern of restoring confidence through policy rate hikes, withdrawal of liquidity, and cuts in the fiscal deficit. The policy response to the pandemic in 2020 has clearly been very different, including policy rate cuts in spite of currency weakness and unconventional monetary easing. EM central banks adopted bond purchase programs (whether formally acknowledged as “QE” or not) to directly finance large government deficits, dampen the effect of increased supply on local bond markets, or as part of liquidity-providing operations.

Consistent with still-sizable excess private savings and expected fiscal consolidation, we have argued that QE is likely

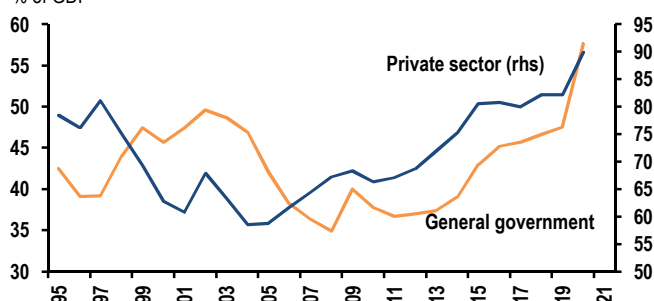
to remain limited this year but could be ramped up in a taper tantrum-type situation to mitigate funding pressures in the bond market. As long as such purchases remain limited and time-bound, much like last year’s experiment, we believe that bond investors are likely to accept such policies and QE could thus be deployed effectively again, reducing local market vulnerabilities further relative to 2013.

Debt level and refinancing needs are the focus of EM vulnerabilities this time around

Fundamental vulnerabilities remain for EM in terms of debt financing needs, which will likely weigh more on hard currency sovereign borrowing than on local markets. Signs of overheating and external vulnerabilities may be lower now versus 2013 but that does not mean there are no fundamental vulnerabilities in EM. EM’s high debt and resulting ongoing financing needs are a vulnerability in a period of less abundant global liquidity. [We have highlighted](#) how 2020 saw the largest-ever annual increase in EM government and private sector debt, which has left these debts at all-time highs (Figure 5). EM government debt is 20%-pts of GDP higher than it was at the time of the 2013 taper tantrum. Yet, many large EM countries have managed to reduce vulnerability to external shocks by shifting debt to local currency, while FX-denominated government debt is increasingly long dated.

Figure 5: EM ex. China debt

% of GDP



Source: J.P. Morgan, BIS, National Statistics, IMF, Haver

Similarly, EM private sector debt has been on a clear rising path over the past decade, but has not been perceived as an immediate concern given that it was dominated by domestic debt and focused in China, although even stripping out China, EM private sector debt is still the highest in 15 years and 15%-pts of GDP higher than in 2013. While large EM countries tend to finance themselves through local debt and will see some fiscal consolidation in 2021, resulting in lower financing needs, many of the smaller frontier EM countries will face ongoing rollover risks.

For large EM countries, debt service metrics remain favorable compared to 2013. Government debt-to-GDP dynamics depend on three factors: the primary fiscal balance (fiscal bal-

ance excluding net interest payments), nominal GDP growth, and the cost of debt service, which, in turn, is a function of interest rates and the maturity of debt. In a taper tantrum environment, the market will naturally focus on the impact of higher interest rates. However, changes in rates take a long time to filter through to debt service costs. The average maturity of EM debt is now about eight years; thus, it takes nearly eight years for changes in interest rates to filter through to the entire debt stock. In contrast, changes in the primary deficit and nominal GDP flow through immediately. The strong post-pandemic growth rebound in implies an average 2021-22 interest-rate-growth differential that is around 100bp lower than during the taper tantrum. Provided GDP growth recovers in line with our forecast and medium-term growth returns to near the pre-pandemic trend, even [a 100bp rise in borrowing costs would leave EM debt on a declining path](#). With respect to the private sector, while credit growth picked up in 2020 in response to policy stimulus, [the pace has remained well below that seen in 2013](#).

But particular attention is warranted for EM frontier markets with high repayment risks. Our assessment continues to be that EM sovereigns are in a default cycle, albeit with a lower default rate in 2021 than in 2020. [We have highlighted](#) countries with higher repayment needs and these will likely see these needs exacerbated by tighter liquidity and higher borrowing costs triggered by a Fed taper. This is a small part of the asset class and if the stress is left to that, should not cause a systemic problem more than a market correction. The bigger risks are from spillover into some of the larger EM countries with high debts, such as Brazil and South Africa. That is why we see debt rather than external imbalances as the likely focus of EM vulnerability from a Fed taper this time around.

Technicals point to less vulnerability

Inflows into EM fixed income funds have slowed significantly since the taper tantrum, with only a small amount being allocated to local markets funds since. The consequence of the lack of inflows from foreigners into EM local markets is seen in the proportion of local bond markets held by foreign investors. This is a common measure of vulnerability, as even if a country manages to issue mostly in its own currency, if the local bond market has sizable foreign investor participation then it is still at risk from outflows. Foreign ownership has fallen across EM on average and has fallen for all the high-yield local markets shown in Table 2, with particularly large declines in those that had higher ownership. A rush to the exit for a country like Turkey is unlikely to be a stampede this time around, given foreign investors now own only 4.0% of the local bonds outstanding versus 25.3% in 2013.

Table 2: Foreign ownership has fallen in the EM high-yielders

Foreign ownership of local bonds

	Brazil	India	Indo	Mex	Russia	S. Africa	Turkey
May 2013	13%	2%	34%	37%	28%	38%	25%
Latest	10%	2%	25%	22%	24%	30%	4%
Change	-4%	0%	-9%	-15%	-4%	-8%	-21%

Source: J.P. Morgan, national sources

EM assets are not expensive compared to pre-taper tantrum pricing, with spreads wider and EM FX weaker. There are concerns that high valuations for other risk assets at a time of still-impaired fundamental conditions might indicate liquidity bubbles. But EM fixed income does not see those conditions. EM currencies may have recovered from their 2020 lows but are 30% weaker versus the USD than they were in 2013. EM sovereign spreads are still 60bp above their pre-COVID-19 levels and over 100bp higher than in early 2013. And while EM local bond yields are lower than in 2013, EM real yields (adjusted for inflation) are much higher versus DM real yields than they were in 2013 when this differential got close to zero.

Conclusion and risks

We do not think that EM assets or fundamentals are vulnerable in the same way they were in 2013. EM weakness likely to follow from a Fed taper decision should not lead to another multi-year bear-market for local markets. EM fundamentals do not have the same overheating signs or external imbalances as 2013, technicals are in a very different place with no large local market inflows, and FX and rates are better-priced currently. Focus this time around is likely to be on hard currency bonds of frontier countries that have ongoing liquidity needs, rather than local FX and rates that needed to correct in 2013 due to external imbalances. Official support may be key to helping fill the financing needs of those countries.

Risks for a more abrupt adjustment in EM may come from a faster rise in US inflation or EM idiosyncratic risks coinciding with uncertainty on global liquidity conditions. A tightening of financial conditions always comes with uncertainty and few predicted the impact on EM of the 2013 taper talk. One set of risks could come from inflation consistently surprising to the upside in the US given the large fiscal stimulus and strong recovery expected. That would quickly bring into question the tolerance of the Fed even under its new inflation averaging framework and is likely to lead to more market weakness with EM hit harder. Alternatively, there is always the possibility that some idiosyncratic risk outcomes in large EM countries (e.g., fiscal risks in Brazil, monetary policy risks in Turkey) coincide with the period of rising US real yields, creating a negative picture for EM more broadly that is more systemic.

Economic Research Note

EM Asia's policy to lean on
core as headline CPI heats up

- EM Asia headline CPI inflation to return to above pre-COVID-19 levels by 2Q21 as supply-side prices firm
- Despite the headline inflation rise, we expect central banks to remain on hold, focusing on core inflation
- Core prices broadly reflect developments in slack; tracking the labor market recovery will be key
- Employment recovery and financial stability will place North Asia at the forefront of policy normalization

The J.P. Morgan forecast pencils in a rise in EM Asia headline inflation to 2.3%*o*ya by 2Q21 from 0.6%*o*ya in December and for it to remain around 2%*o*ya through 2H21 (Figure 1). This puts headline inflation above pre-COVID-19 rates, reflecting a combination of base effects and the rise in supply-side prices, especially energy, with Brent crude expected to reach US\$68/bbl by year-end. By contrast, the trajectory for core inflation pencils in a more gradual rise to reach 1.4%*o*ya by end-2021 from 0.9% in December. Despite the rise in headline inflation, we expect that central banks will remain on hold through 2021, focusing on core inflation rather than headline (Figure 2). Indeed, a rapid rise in supply-side prices without a concomitant economic recovery could dent real purchasing power, which should prompt some caution in tightening monetary conditions.

Figure 1: EM Asia headline and core CPI

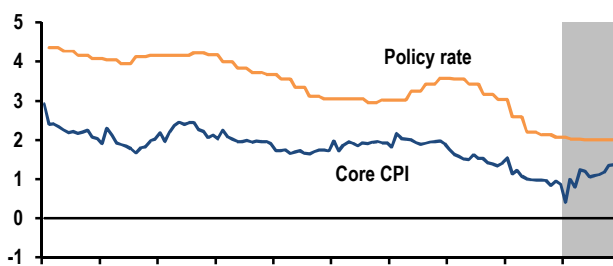
%*o*ya, equal weighted

Source: National sources and J.P. Morgan forecasts in shaded area

This view of slow-moving central banks is premised on the judgment that the multi-speed recovery, with services lagging the goods recovery, will deliver a similarly pedestrian recovery in the labor market, thus exerting modest underlying price pressure. Consequently, a focal point will be labor market developments. A faster-than-expected labor market recovery could prompt us to bring forward policy normalization. In this context, we expect that North Asia—given the faster pace of

recovery from the COVID-19 shock, smaller exposure to travel-related services, and rising concerns around [financial stability](#)—would lead the region in [normalizing policy](#).

Figure 2: EM Asia core CPI and policy rate

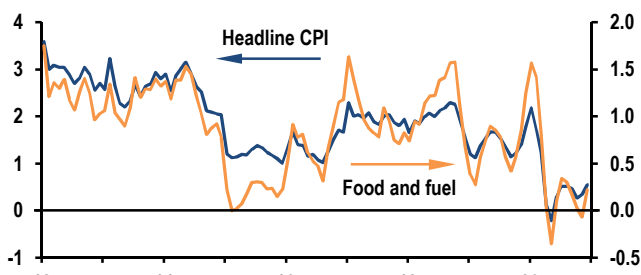
%*o*ya and %*p.a.*, eop, equal weighted

Source: National sources and J.P. Morgan forecasts in shaded area

Some observations of headline and core inflation

One striking aspect of Emerging Asia is the large influence that supply-side prices have on inflation, with food and fuel prices primarily explaining swings in headline inflation (Figure 3).

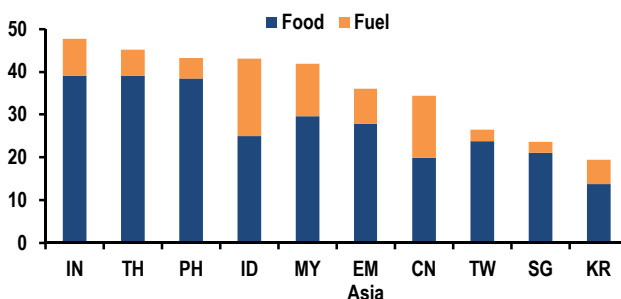
Figure 3: EM Asia headline CPI and food and energy prices

%*o*ya, equal weighted%pt. contribution to %*o*ya headline CPI

Source: National sources

Figure 4: EM Asia CPI weights of food and fuel

% of CPI basket



Source: National sources

This owes to the relatively large share of food and fuel in the CPI basket, which averages around 35% of the total for EM Asia, comprising 27% food and 8% fuel (Figure 4). That said, wide variation in the weights mirrors income levels across the

region, ranging from over 39% of the basket in India to less than 15% in Korea, which means that the influence of commodity prices on overall inflation trends is not uniform. Nonetheless, commodity prices are a dominant influence on regional headline inflation.

However, the focus on headline inflation overlooks the more benign trend in core inflation, especially since 2015. Indeed, regression estimates suggest that supply-side influences on core inflation have ebbed since 2010 while the role of output gaps has grown (Table 1). This in our view mirrors the general slowing of employment growth in the past several years and also informs the inertia of policy rates relative to headline inflation (Figures 5 and 6, and [here](#), [here](#) and [here](#)). Though the high-frequency employment data are only available for a subset of the region, the resonance of these trends is notable across both high-income and middle-income EM Asia.

Table 1: Drivers of EM Asia core inflation

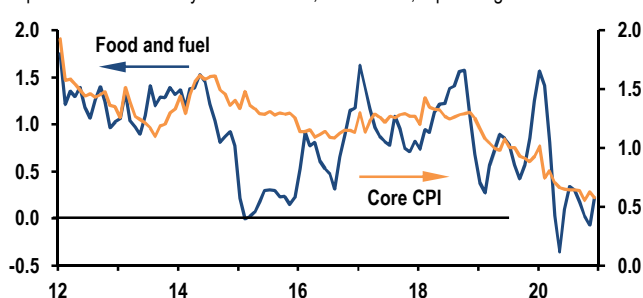
Dependent variable, EM Asia core CPI equal weighted, %q/q, saar

Ind. Variable (lag)	2005-2020		2010-2020	
	Coeff.	P-val.	Coeff.	P-val.
Constant	1.24	0.00	0.90	0.01
Core (-1)	0.49	0.00	0.61	0.00
Output gap (-3)	0.02	0.82	0.23	0.06
FAO food (-1)	0.04	0.00	0.02	0.21
Oil	0.01	0.09	0.01	0.16

Source: J.P. Morgan estimates

Figure 5: EM Asia inflation by source

%pt. contribution to %oya headline CPI, both scales, equal weighted



Source: National sources

Figure 6: EM Asia-5¹ employment income and core CPI

%oya, both scales, local currency terms, equal weighted



Source: National sources; 1. HK, KR, SG, TH, TW

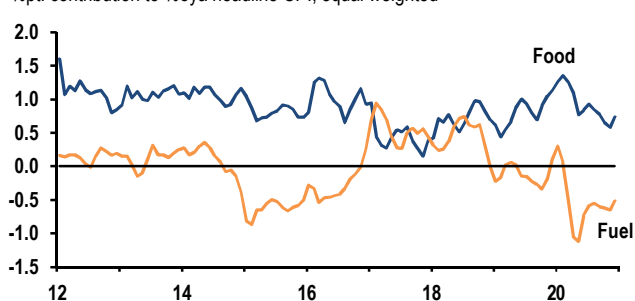
Thus, given the slower-moving path of core inflation, we believe there is no rush for central banks to hike this year, unless slack—proxied by unemployment—decreases much faster than anticipated.

Fuel to add most in 2Q21, with variations

As noted, food and fuel prices tend to dominate the broad contours of headline inflation. However, of the two, fuel prices tend to drive the swings, with food price fluctuations of smaller amplitude. Food contributions to annual headline CPI inflation have been 0.5%-1.5%-pts in the past decade, averaging around 1%-pt. The contribution from fuel prices, while broadly lower than that of food due to its lower weight, is more volatile, ranging between -1%-pt and 1%-pt (Figure 7). We expect headline CPI inflation will firm in 2Q21 with the energy contribution peaking at 1.6%-pt in 2Q21 from the trough of -1%-pt in 2Q20, tracking the profile of crude oil (Figure 8).

Figure 7: EM Asia food and fuel inflation

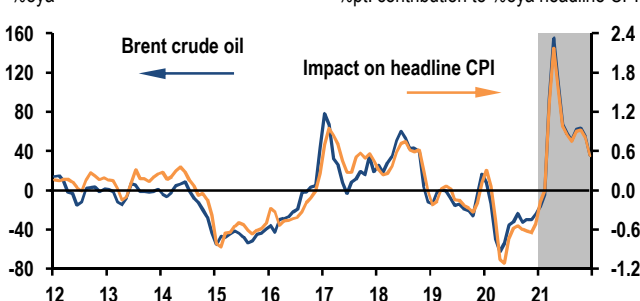
%pt. contribution to %oya headline CPI, equal weighted



Source: National sources and J.P. Morgan estimates

Figure 8: EM Asia Brent crude oil and impact on CPI

%oya %pt. contribution to %oya headline CPI



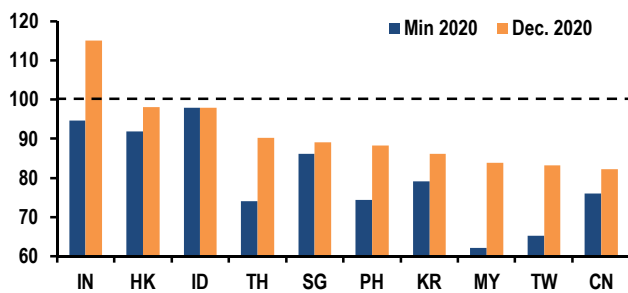
Source: National sources and J.P. Morgan forecasts in shaded area

The pass-through from crude oil prices into pump prices varies across the region, reflecting the impact of different energy policies. Nonetheless, for most of the region, the minimum pump price occurred in April or May of last year, except in China, where it occurred in 3Q20, suggesting that the %oya increases in fuel will be most prominent in 2Q this year, especially in economies with the lowest pump prices in 2Q20

(Malaysia, the Philippines, Taiwan and Thailand), thus amplifying the over-year-ago comparison (Figure 9).

Figure 9: EM Asia retail fuel pump price

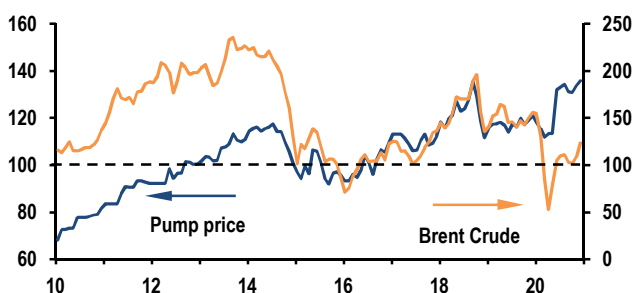
Jan 2020=100, local currency terms



Source: National sources

Figure 10: India crude oil and domestic pump price

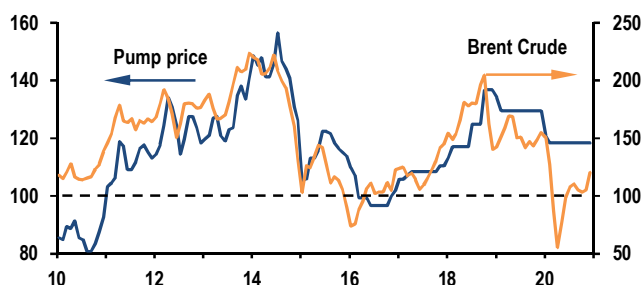
Index, 2016=100, local currency terms, both scales



Source: IOCL

Figure 11: Indonesia crude oil and domestic pump price

Index, 2016=100, local currency terms, both scales



Source: BPS

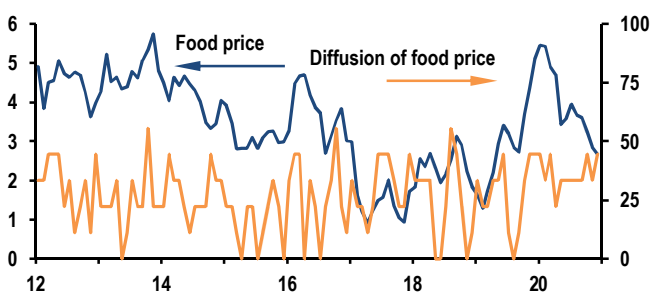
Across the region, India and Indonesia stand out in terms of the limited pass-through of the drop in crude oil prices into retail prices. India still had higher pump prices in December than in January last year, with the savings from lower oil prices accruing to the public sector (Figure 10). Similarly, the decline in energy prices has barely been passed through to pump prices in Indonesia (Figure 11). What this implies is that the shock from higher oil prices is already being felt in India even as food prices ease, while in Indonesia, current retail fuel prices are likely to be calibrated to a crude oil price range of US\$63-68/bbl, and thus will not need to be adjusted until crude oil prices reach around US\$70/bbl.

Food prices driven by regional idiosyncrasies

Food inflation in the region tends to be idiosyncratic, with the food price shock in China and India last year not observed elsewhere (Figure 12).

Figure 12: EM Asia food CPI and diffusion

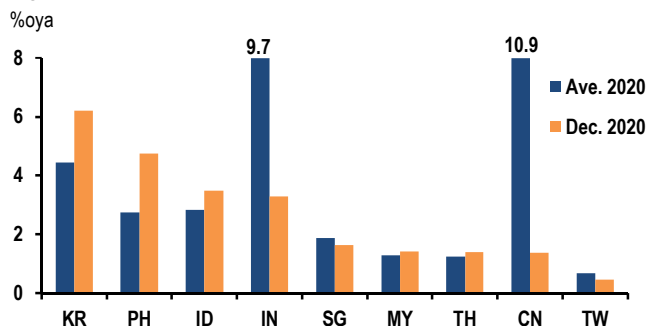
%oya, equal weighted % of region with food rising in %oya over 2-mos. rolling



Source: National sources and J.P. Morgan estimates

Indeed, the relatively narrow breadth of the regional food diffusion index suggests limited broader propagation of common food price shocks across the region. Moreover, it is fresh food, which is particularly susceptible to weather-related disruptions, rather than processed food that generally drives the contours of overall food prices. This weather dependence thus complicates our ability to forecast country-level food prices accurately. That said, food prices have recently firmed in Korea, due to fruit prices, and in the Philippines, due to meat and vegetable prices (Figure 13).

Figure 13: EM Asia food CPI

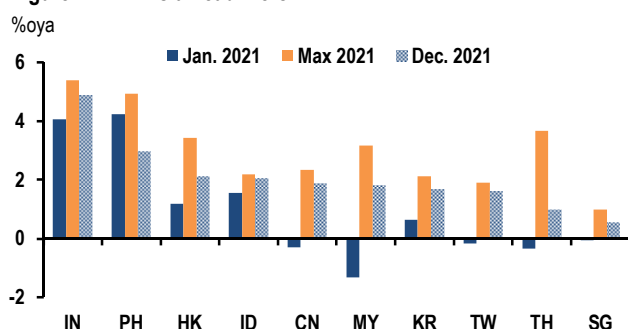


Source: National sources

Headline CPI heading up, core too; leading to policy divergence

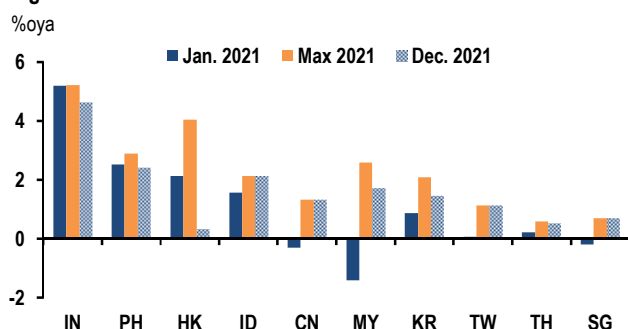
Given the expected trajectory of food and fuel prices, the general contours of annual headline inflation suggest a peak in 2Q21 before readings subside a touch by year-end as the base effects in over-year-ago comparisons fade (Figure 14). Similarly, we expect that core inflation too will rise as the recovery evolves though it should rise less steeply than headline inflation (Figure 15).

Figure 14: EM Asia headline CPI



Source: National sources and J.P. Morgan forecasts for max and end-2021

Figure 15: EM Asia core CPI

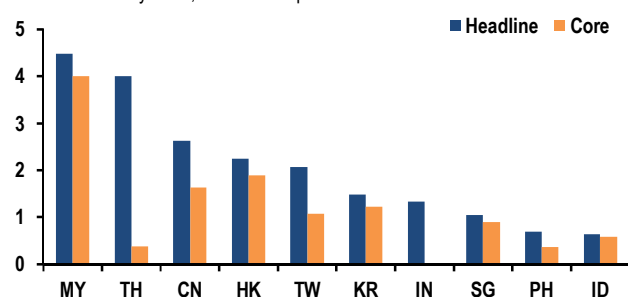


Source: National sources and J.P. Morgan forecasts for max and end-2021

In terms of relative changes in over-year-ago headline inflation readings, we expect the largest increases between January and the 2021 peak in Malaysia (April), Thailand (May) and China (November) due in large part to energy price effects, as noted previously, and the smallest in Singapore, the Philippines (due in part to the already elevated readings from the rise in food prices) and Indonesia (Figure 16). By contrast, we expect the changes in annual core inflation to be less than headline CPI for most of the region.

Figure 16: EM Asia changes in CPI

Difference in %yoy CPI, Jan to 2021 peak

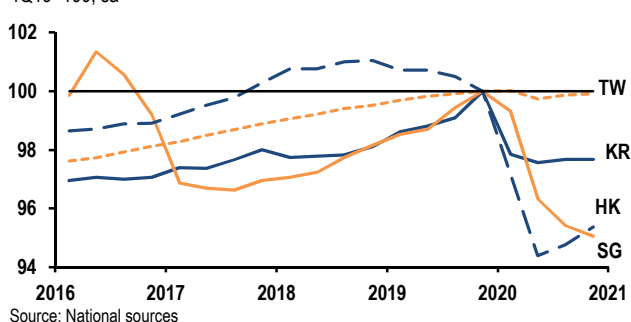


Source: National sources and J.P. Morgan forecasts for max and end-2021

with labor markets a useful proxy for underlying slack (Figure 17).

Figure 17: EM Asia employment

4Q19=100, sa



Source: National sources

The divergent trajectories of employment already reveal notable differentiation across the region, with the North Asian manufacturing bellwethers clearly on the mend even as employment in ASEAN has yet to turn the corner, though we do expect an acceleration in late 2H21 as vaccination progress accelerates in 2H21 and borders gradually open. Although we have not penciled in rate hikes this year, should employment continue to firm solidly, core inflation rise, and asset inflation broaden, this could tip monetary policy in North Asia toward normalization, leading the region given the smaller output gaps relative to the rest of the region.

Focus on labor markets

Despite the ostensible rise in headline inflation, we anticipate that the focus for policy normalization will be on output gaps,

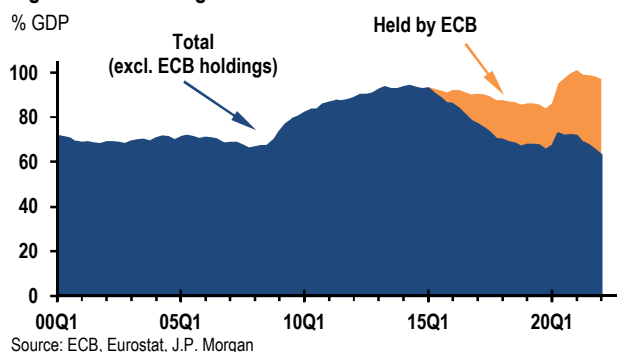
Economic Research Note

ECB debt cancellation is a bad idea

- **ECB is set to hold a third of Euro area government debt by 1Q22**
- **There are calls to cancel the ECB's holdings to unleash a large expansion in government investment**
- **The ECB is already reducing governments' debt burdens via low rates and asset purchases**
- **Debt cancellation would make ECB's support permanent, but only by creating huge problems**

In recent years, there have been frequent calls for a significant part of Euro area government debt to be written off. This has often been focused on the debt of individual Euro area countries, but attention has also turned to the ECB. This is not surprising as the ECB will hold around a third of all outstanding government debt by 1Q22 if it makes full use of the current €1,850bn PEPP envelope (Figure 1). In terms of the impact on governments' debt burden, the difference between a cancellation of the ECB's bond holdings and the support the central bank is already providing through its asset purchase programs is quite nuanced. However, debt cancellation creates much more fundamental problems that make this option very unattractive and highly unlikely in practice.

Figure 1: Euro area government debt



The latest call for debt cancellation

A recent [call](#) to write down the ECB's holdings of sovereign debt illustrates the issues that this raises. This proposal calls for a deal between Euro area governments and the ECB to cancel the sovereign debt (or transform it into perpetual debt with 0% interest). Governments would then commit to using their new fiscal leeway to invest an amount equal to the canceled debt in social and ecological projects. The proponents of this argue that the ECB can "afford" this because it can operate with negative capital "without difficulty." They also argue

that this is not forbidden by the EU Treaty and that the ECB could even print money to compensate for the losses. On the latter, proponents refer to Protocol 4 that is annexed to the EU Treaty. They recognize that governments may not want to invest as much as the €2.5 trillion (20% of GDP) that they think is necessary for a "social and ecological recovery plan." After all, even a long period of negative ECB policy rates has not sharply increased government investment. But, they hope the fiscal leeway that would be achieved through ECB debt cancellation would create political pressures to actually spend that money.

Is there really a free lunch?

Would debt cancellation by the ECB amount to a free lunch for the economy? We have written about this [before](#), but it is instructive to consider the mechanics again (Table 1). On the asset side of its balance sheet, the ECB has holdings of gold, foreign reserves, loans to banks (e.g., TLTROs), domestic assets bought under the asset purchase programs, and a large amount of "other assets." On the liability side, the ECB funds these asset holdings by issuing banknotes and reserves to banks and by holding capital/reserves. The ECB also has a large revaluation account, which reflects mark-to-market gains, mainly from the price of gold.

Table 1: Latest ECB balance sheet

€ bn			
Assets		Liabilities	
Gold and FX-related	913	Banknotes/coins	1433
TLTROs, etc.	1793	Reserves	3704
Asset purch. (APP, PEPP)	3832	Other liabilities	1344
Other assets	563	Revaluation accounts	513
		Capital/reserves	108
Total	7101	Total	7101

Source: ECB, J.P. Morgan

How would the ECB's balance sheet change if €2.5 trillion of government bond holdings were canceled? On the asset side, the holdings under the asset purchase programs (APP, PEPP) would fall by that amount. On the liability side, the ECB's capital position would be wiped out (i.e., set to -€2,392bn).

Table 2: ECB balance sheet after a €2.5 trillion debt cancellation

€ bn			
Assets		Liabilities	
Gold and FX-related	913	Banknotes/coins	1433
TLTROs, etc.	1793	Reserves	3704
Asset purch. (APP, PEPP)	1332	Other liabilities	1344
Other assets	563	Revaluation accounts	513
		Capital/reserves	-2392
Total	4601	Total	4601

Source: ECB, J.P. Morgan

Figure 2 illustrates the relevant mechanics using stylized balance sheets of the ECB and the banking system. In Step 1, the banks own 100 of government bonds. In Step 2, the ECB launches an asset purchase program to stimulate the economy and buys the bonds from the banks by creating reserves. The banks used to hold government bonds and now hold reserves instead. In Step 3, the ECB writes down the bonds, which makes its capital position negative. But, the ECB still has a liability to the banks in the form of the reserves it created when it first bought the bonds. (As an aside, note that the banks have no choice but to hold these reserves as the system for reserves is closed: Bank A can try to get rid of its reserves, for example by buying an asset, but this will only transfer the reserves to Bank B through the payment system).

Figure 2: Sovereign QE and debt cancellation
€

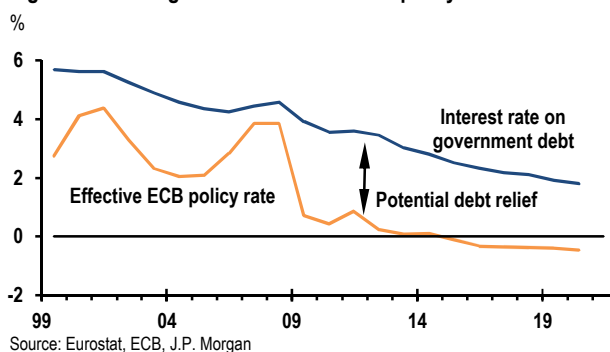
Step 1: Starting position			
ECB		Banks	
Assets	Liabilities	Assets	Liabilities
Govt debt: 0	Reserves: 0 Capital: 0	Reserves: 0 Govt debt: 100	
Step 2: ECB buys government bonds from banks to stimulate economy			
ECB		Banks	
Assets	Liabilities	Assets	Liabilities
Govt debt: 100	Reserves: 100	Reserves: 100 Govt debt: 0	
Step 3: ECB cancels its holdings of government bonds			
ECB		Banks	
Assets	Liabilities	Assets	Liabilities
Govt debt: 0	Reserves: 100 Capital: -100	Reserves: 100 Govt debt: 0	

Source: J.P. Morgan

How does this affect the flow of interest payments? In Step 1, the bonds that the government has issued are held by the banks and therefore the government pays interest on these bonds to the banks. In Step 2, the government makes interest payments to the ECB, which now holds the bonds, while the ECB pays interest to the banks on the reserves it has created. The interest on the reserves is the ECB's overnight policy interest rate, which will be lower than the longer-term interest rate that the government pays to the ECB on the government bonds. Hence, the ECB makes a profit on the interest rate differential, whereas the banks now have a lower-yielding asset (i.e., reserves). The ECB's profit on this interest rate differential (i.e., the term premium) largely is returned to the governments at the end of the year in the form of distributed profits. In Step 3, the government no longer pays interest on the canceled debt, but the ECB still has the liabilities (i.e., reserves) it created when it bought the bonds in the first place. In essence, the ECB still has the liabilities after the debt cancellation but it has no assets to generate income.

How does this reduce the governments' debt burden? From a debt servicing perspective, purchases of bonds by the central bank already provide relief to governments via two channels. First, bond purchases by the ECB effectively transform long-term government debt into short-term debt (i.e., reserves that have an overnight maturity). Figure 3 shows that the effective interest rate that Euro area governments pay on their debt was around 1.8% in 2020, which equates to a fiscal cost of almost 1.8% of GDP (given that government debt rose to around 100% of GDP). The ECB holds a quarter of this debt and effectively funds this through reserves at an interest rate of -0.5%. The profit made on this interest rate differential with the policy rate is returned to the governments at the end of the year, saving governments around 0.5% of GDP. Second, ECB asset purchases have also reduced long-term interest rates by compressing the term premium, which reduces the debt servicing costs on the 75% of the government bonds that is still held by investors.

Figure 3: Sovereign interest rate and ECB policy rate



Source: Eurostat, ECB, J.P. Morgan

Given that assets purchases have already significantly reduced governments' debt burdens, what additional impact would a debt cancellation have? If the sovereign debt held by the ECB is not canceled, then the ECB can use some of the interest it receives from governments to pay interest on the reserves it has created and only returns the difference to the governments as profit. By canceling the debt, governments save even more as they reduce their interest payments on the bonds held by the ECB all the way to zero. The other effect of a debt cancellation is that it locks in forever the reduction in the debt servicing burden. This is because the ECB may at some point sell bonds back into the market when it normalizes policy, but cannot do so if it has canceled the debt. In that case, governments would no longer be exposed to the risk of having to make interest payments to the private sector and no longer receive a part of its debts service payments to the ECB back in the form of "distributed profits." In this sense, debt cancellation could also be achieved by transforming the government bonds held by the ECB into perpetual bonds or if the ECB commits to rolling over its current bond holdings forever.

So, what's the problem with this?

The discussion so far suggests that regular asset purchases by the ECB already provide significant debt relief to governments in the form of reduced debt servicing costs. It also suggests that the additional change from a formal debt cancellation can seem nuanced, at least as long as the ECB's balance sheet is still large. But, does that equate debt cancellation to a free lunch and are there broader costs from such a move? In brief, it would not and, in fact, it would create very fundamental problems, which makes it very unattractive and unlikely.

Crucially, a debt cancellation would confront the ECB with a set of difficult choices. As noted above, the ECB would be left with large liabilities (i.e., reserves) and few assets to generate income. If the ECB is uncomfortable with having a very negative capital position, it can try to rebuild its capital over time by setting the interest rate on reserves lower than it otherwise would. That could involve changing the regulatory framework so that banks are required to maintain high levels of reserve holdings without those reserves receiving interest when rates are in positive territory. While this would lower the ECB's interest costs it imposes a loss of revenue on the banks who are likely to pass this on to their customers. The other option for the ECB is to pay banks the normal interest on reserves, and to do so by "printing money" (i.e., by simply crediting banks' reserve accounts with new reserves). This second option could ultimately lead to exponential increases in the supply of high-powered money, as more interest-bearing reserves are created to pay the interest on the existing stock of reserves.

Even if the ECB chooses the first option, which is a form of financial repression, the possibility that it could at some point resort to printing money creates the risk of unstable outcomes. From a technical perspective, the ECB would still be able to pursue its price stability mandate as it could still set interest rates, buy/sell assets, and lend to banks. But, a debt cancellation could create significant doubts about the ECB's ability to take tough decisions and resist political pressures. And once the bonds held by the ECB have been canceled once, there would be an expectation that they can be canceled again in the future. That risk could make the ECB reluctant to engage in asset purchases that could be needed in a future downturn. More broadly it raises questions about the stability of macroeconomic policy and the extent to which monetary policy will remain be made to serve a fiscal purpose rather than pursuing price stability. In turn, such a regime shift can lead to unpredictable behavioral responses of households, corporates, and investors in general (including foreign ones). This could manifest itself in large changes in exchange rates, saving rates, and inflation expectations.

In our view, there is also a real risk that a cancellation of the government debt held by the ECB would not have the positive effect on confidence and government investment that some advocates of the policy hope for. In fact, the reverse may be the case. The region is at delicate point in its political and institutional evolution: the ECB's OMT and PEPP programs have pushed the envelope on how far central bank support for sovereign financing can go, while the regional recovery fund makes a clear step in the direction of more systematic income transfers within the EU and euro area more specifically. For many Northern European countries, cancellation of debt held by the ECB would cross a red line and could undermine support for the entire monetary union. The never-ending debate in Germany about the TARGET2 imbalances can be seen as a reflection of this as it reveals an underlying skepticism and mistrust of monetary solutions to real economy problems. For this reason, a cancellation of the government bonds held by the ECB would be a nonstarter politically.

One can claim that, since the ECB's holdings of debt are broadly in line with its capital key, there would not be a significant distributional effect from a debt writedown. However, there is little doubt that such an action would be seen as more "beneficial" to countries facing risks associated with a high debt burden rather than those with low debt, even if the sums involved were the same when scaled by GDP.

There is also the question of legality. As is clear from the challenges to the ECB's asset purchases that have gone through the German Federal Constitutional Court, there can be huge debates about how exactly to interpret the prohibition on monetary financing. In this context, it matters however that a number of ECB policymakers, including President Lagarde, have already dismissed the debt cancellation proposal as illegal.

There is also a final question, which is about the true constraint on higher government investment. Financing conditions facing Euro area governments are already very easy and this has failed to trigger the sharp increase in government investment that the advocates of a debt cancellation are calling for. It is therefore unclear if a large-scale cancellation of government debt through the ECB would change this in practice.

Economic Research Note

Euro area: Core inflation lift this year largely temporary

- **Three factors explain the 1.2%-pt January rise in core inflation; these effects will disappear next year**
- **Stickiness to swamp bottlenecks, speed effects, and input price pressure**
- **Core inflation should return to pre-virus level by end-2022, as slack diminishes and inflation expectations rise gradually**

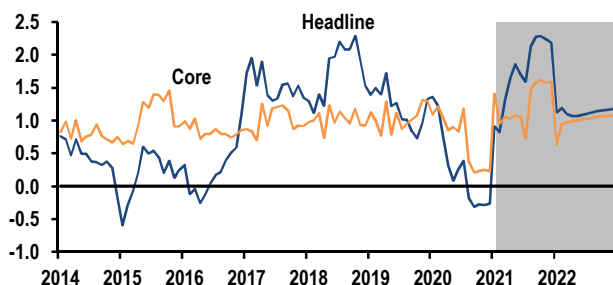
The sharp move up in Euro area inflation at the start of the year was unprecedented. Core inflation jumped 1.2%-pts to 1.4%oya and the rise in headline inflation was equally strong (+1.2%-pts to 0.9%oya). Many factors contributed to this jump, including the reversal of the German VAT cut, delayed winter sales, new weights in the HICP basket, and the rise in the price of Brent. In our view, these factors will have a transitory impact on core inflation this year, as we describe below.

In the broader reflation debate, additional factors may play a role this year, including rising input prices, bottleneck pressures, and speed limit effects. These factors add upside risk to our forecast but we think a predominant feature of Euro area prices—stickiness—largely will prevail.

Overall, we expect core inflation to hover around 1.1%oya during the rest of 1H21 (Figure 1), before rising to 1.5% in 2H21 due to a base effect linked to the German VAT cut last year. As the impact of transitory factors fades at the start of next year, we think core inflation will decline to 0.9%oya in 1Q22. The gradual rise in core inflation to 1.1% by the end of next year in our forecast—i.e., back to the pre-virus level—is driven by the reduced slack and a gradual move up in inflation expectations.

Figure 1: Euro area HICP inflation

%oya (shading denotes forecast)



Source: Eurostat and J.P. Morgan

Transitory factors at play

The rise in core inflation last month was driven by a range of factors that will influence core inflation during the year, but eventually will fade at the start of next year. As HICP details were released this week, we are now able to decompose the January move and provide insights for the coming months:

- **German VAT rate back to 19%.** The German VAT rate was lowered from 19% to 16% last July. This move was temporary and the VAT rate returned to its pre-virus level at the start of the year. We estimate that the temporary reduction in the VAT rate in 2H20 lowered Euro area core inflation by 0.4%-0.5%-pt. The return to 19% now means that the drag disappeared. It also means that a base effect will lift Euro area core inflation by about 0.4%-0.5%-pt in 2H21, which largely explains the rise in our core inflation forecast in the second part of the year.
- **Delayed sales period lifted core in January.** The increase in clothing and footwear price inflation from December to January was huge, from -2.2%oya to 2.5%oya, lifting Euro area core inflation by nearly 0.4%-pt. This increase to some extent is linked to the German VAT rebound, but a closer look at the details shows that clothing and footwear price inflation also jumped in France, Italy, and Austria. As we already mentioned, winter sales were delayed in some countries and prices did not fall as much in January as the normal seasonal pattern would suggest. This rise is temporary and will have dissipated by March. Meanwhile, it is possible that this category becomes a drag on core inflation in February, but this is not the pattern that was seen last summer when sales also were delayed in some countries.
- **Weight changes are a boost.** The HICP basket changes every year to reflect consumption patterns in the region. And last year, the fall of consumption in some categories was large, including restaurants, hotels, and transport. We already discussed how weight changes can have a [significant impact](#) on inflation using the preliminary German data. Using Eurostat's methodology, we calculate that new weights lifted Euro area core inflation by 0.4%-pt. How this effect plays out during the rest of the year is unclear as the impact depends on the interaction of weight changes and price changes (some of which can be very volatile). We nonetheless [presented a scenario](#) where the impact could fade by the summer, before turning negative for a few months, and then become positive again around year-end.
- **Data collection issues had limited impact.** We had mentioned that data collection issues were still significant but that the impact of this factor would likely be limited. Indeed, 18% of core items had to be imputed in January as prices could not be collected. But the impact would have

been small since the factors we discussed above already explain the January jump in core inflation.

Risk factors to consider

A number of additional factors are also important to consider this year when thinking about the broader reflationary theme. These factors add upside risk to our forecast:

- Rising input and output prices.** In last week's PMI release the manufacturing input price index stood at its highest level since 2011 and price pressures are being reflected in output prices. According to the survey, supply-side constraints (including cargo shortages and microchip shortages) have raised input prices. But higher commodity prices in general, boosted by higher demand, also had a significant impact (Figure 2). Nevertheless, the correlation between the PMI manufacturing output price index (or commodity prices) and core goods price inflation is weak (Figure 3). It is not clear that rising input prices will feed through into consumer prices and corporates may continue to absorb rising costs in their margins. One specific channel would be how oil prices feed into airfares, but even this channel would have a modest impact on core inflation overall and is being dampened by the lower weight of airfares in 2011.

Figure 2: Manufacturing PMI output prices and commodity prices

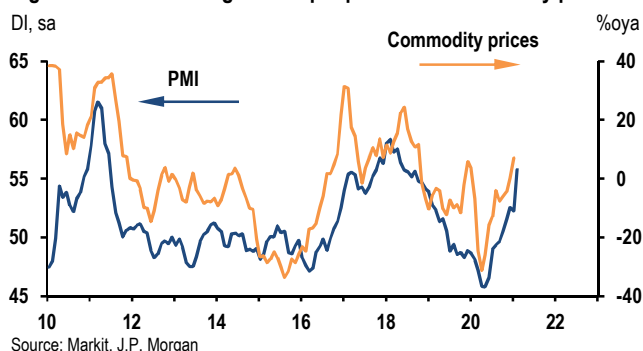
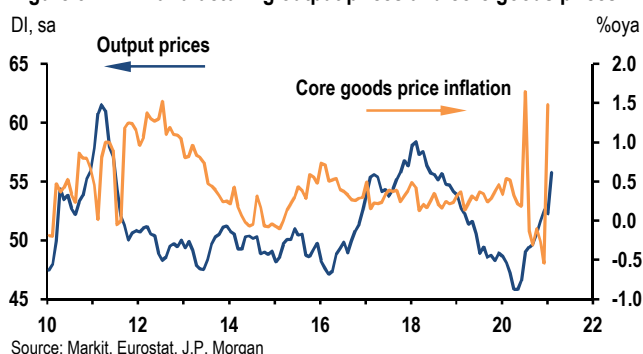


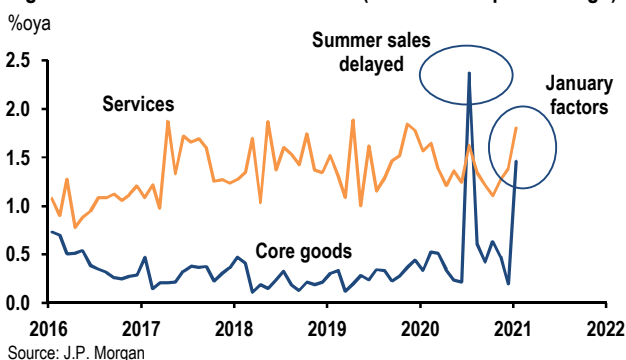
Figure 3: PMI manufacturing output prices and core goods prices



- Potential bottleneck issues from spring onwards.** Some services sectors (including the hospitality and leisure sec-

tors) have been hit hard by restrictions. And the fall in core inflation this year was to a large extent driven by the holiday categories (airfares, package holiday prices, accommodation services). As restrictions are relaxed in coming months, demand may be particularly strong in some sectors with potential bottleneck issues. The inflation consequences could be significant in the holiday sector where prices can be very volatile due to seasonality. We note however that, contrary to the US experience, Euro area core goods price inflation did not rise in 2H20 as goods demand surged, even if we control for the impact of the German VAT cut (Figure 4). Bottleneck issues may thus be less powerful in boosting inflation in the Euro area than in the US.

Figure 4: Inflation at constant tax rate (assumes full passthrough)



- Speed effects not significant.** Our Phillips curve framework assumes that core inflation depends on the level of the output gap, but in a context of a rapid pickup in activity it is legitimate to ask whether inflation could respond to changes in the output gap. We will investigate this issue further but our first stab at testing for this hypothesis using our forecasting framework shows that speed effects are not significant in the Euro area. Looking specifically at the 2010-2011 period, our model is able to explain the sharp rise in core inflation only using the level of the output gap. We furthermore note that core inflation remained remarkably sticky last year while the output gap collapsed in an unprecedented way.

A fall followed by a gradual rise next year

As the impact of temporary factors fades at the start of next year, we expect Euro area core inflation to drop to 0.9%oya in 1Q22. In contrast to the US experience, Euro area core inflation has been remarkably sticky in the last 12 months, while the economy has faced an unprecedented shock. We expect this stickiness also to prevail next year with core inflation slowly returning to its pre-virus level by the end of next year. In our forecast the reduced level of slack and a gradual increase in inflation expectations lift core inflation to 1.1% in 4Q22.

Economic Research Note

UK: The rising fiscal impact of changes in the policy rate

- QE makes government debt servicing costs more dependent on the BoE's policy rate
- This sensitivity has increased since the pandemic
- Some argue this will threaten BoE independence when rates eventually rise
- But context matters, and any such challenge would not be without cost

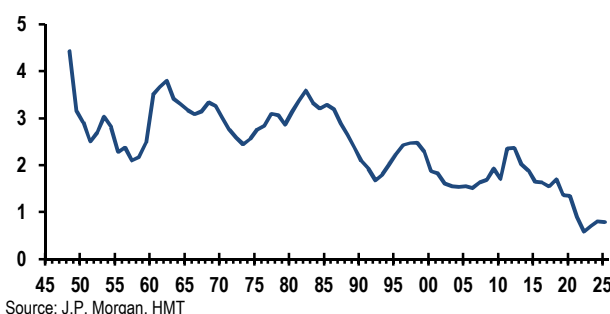
Following substantial support during the pandemic, the BoE's holdings of total government debt will have risen from around a quarter to more than one-third by the end of this year. This has delivered a number of benefits for the government, most notably the prevention of a large spike in borrowing costs. But QE also means that government debt servicing costs have become more closely linked to the BoE's policy rate, in effect enabling the government to borrow at the short term rate of interest. This benefit is likely to go into reverse when rates begin to rise, with debt servicing costs rising as interest paid on reserves increases. This has prompted some to argue that BoE independence eventually could be called into question, as higher rates would essentially place the public finances on a worse footing all else equal. But the political strain this causes will depend on how well the economy is doing at the time, and any potential challenge to central bank independence would not be without cost. In this note we put some numbers on the impact in question, noting that the sensitivity of government net interest payments to a 100bp increase in the policy rate has risen to 0.8% of GDP.

How QE has changed debt servicing costs

Viewed from the perspective of the consolidated public sector balance sheet—i.e., combining the accounts of the government and central bank—government debt interest payments on gilts held by the BoE essentially become linked to the policy rate. That's because gilt coupon payments made by the government are collected by the BoE and then mostly handed back to the government. This means the overall impact on the public sector finances of the coupon payments associated with these liabilities is almost zero. The cost of servicing this portion of government debt is instead driven by the policy rate, as this is the rate at which the BoE remunerates the reserves it created when these purchasing gilts. Viewed from this perspective, gilts held by the BoE have effectively had their maturity reduced to near zero, i.e., they are funded at ultra-short term rates and without rollover risk.

Figure 1: Government debt net interest costs

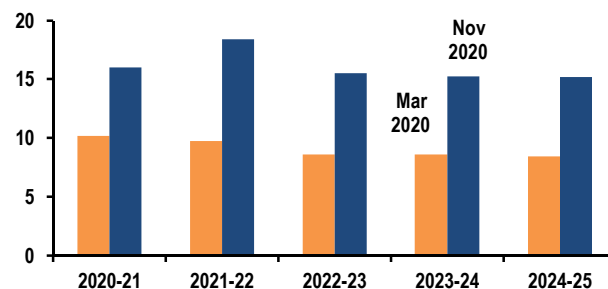
% of GDP, includes OBR forecast from 2020



The impact of this has so far been very beneficial for the government, and has played a crucial role in helping to drive down the net interest burden to multi-decade lows (Figure 1). As a consequence of the BoE's gilt purchases the amount of interest the government pays on its debt has been reduced by around £15bn per year, or 0.7% of GDP. This saving has increased since the pandemic (Figure 2) as the BoE cut rates 65bp and announced a near doubling of its asset purchases. This demonstrates the additional benefit to the government of having a large part of its debt stock held by the central bank.

Figure 2: Reduction in government borrowing costs from QE

£bn, reduction in net debt interest associated with QE



This also demonstrates the sensitivity of the public finances to changes in the BoE's policy rate. While this has so far been a benefit to the government, at some point in the future the opposite will be true, with higher BoE rates raising government debt interest expenditure. A higher Bank Rate would mean higher interest being paid out on reserves, and would mean the BoE handing back less of the coupon payments it receives from its gilt holdings to the government. Table 1 below shows the OBR's estimate of the sensitivity of the public finances to changes in key economic variables, and how they have changed over time.

Table 1: Sensitivity of government debt interest payments

% of GDP, sensitivity to a 1%-pt rise in listed variables

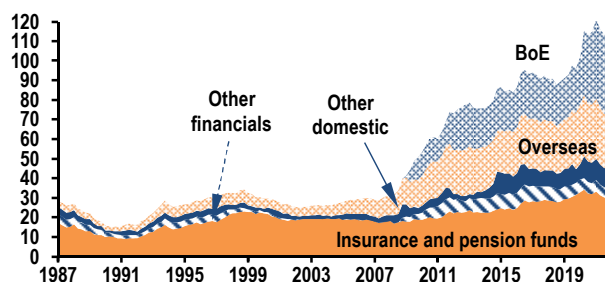
	Dec 12	Nov 16	Mar 20	Nov 20
Gilt rates	0.37	0.22	0.24	0.33
Short rates	0.16	0.24	0.23	0.45
Inflation	0.29	0.29	0.25	0.27

Source: OBR, DMO

Net interest payments on debt will rise with short rates for the reason described above. But this is also true with longer-term gilt rates, as the majority of government debt still lies outside the BoE's asset purchase facility and hence will also need to be refinanced at higher rates (Figure 3). If the BoE does raise its policy rate, this will not just increase government interest payments due to higher outlays on reserve remuneration, but will also push up rates across the yield curve. If we add together these two elasticities a 1%-pt rise in rates across the curve is estimated to lift debt servicing costs by almost 0.8% of GDP. This is likely to increase further as the BoE completes its remaining £150bn tranche of QE. In the fairly short space of time since the pandemic began, this sensitivity has risen from a 0.5% average seen prior to 2020. The sensitivity to short rates is now also greater than that of gilt rates.

Figure 3: Gilt holdings by sector

% of GDP, includes JPM forecast based on policy announcements



Source: J.P. Morgan, HMT, OBR

Potential conflict when rates rise

The closer relationship between government borrowing costs and the BoE rate has led to concerns that the central bank's independence could be in jeopardy when rates eventually do rise. A tightening in monetary policy would, all else equal, increase the fiscal deficit. To achieve a given objective for the deficit, therefore, the government would either have to raise taxes or cut other forms of spending. For example, the BoE has previously suggested that the longer-term equilibrium policy rate might be 2%-3%. This would amount to a rate increase of around 250bp, pushing up debt interest payments by 2% of GDP.

While this figure is significant, the political challenges it creates would depend very much on context. Higher rates might be needed to prevent an inflation overshoot even if the growth

backdrop remains weak. In this scenario there would be little mitigation of the rise in borrowing costs. Indeed, a challenging macroeconomic backdrop would also weaken tax receipts and put the public finances under even greater strain. In contrast, if rate increases happened in response to an unexpected pickup in growth, the resulting rise in government borrowing costs would at least partly be mitigated by the favorable impact of a stronger economy on the tax take. As a rough rule of thumb, each 1%-pt upside surprise on GDP might be expected to reduce the deficit by 0.7% of GDP.

What can the government do?

Some prominent economists—including one former MPC member and a former BoE chief economist—have argued that the sensitivity between future interest rate increases and the public finances could challenge central bank independence. This could reveal itself in a number of ways, including MPC member appointments, changes to the BoE's mandate, and public statements from the government. Some of these interventions would be more overt than others. But if the government made a clear attempt to prevent a monetary tightening necessary for the BoE to meet its inflation target, there likely would be a strong reaction in financial markets—with inflation expectations rising and a risk of lasting damage to hard-won credibility. In this sense there would be no painless option for the government.

Independently of the conflict we describe in this note, there have been calls for central bank inflation targets to be increased to ease the policy constraints posed by the zero lower bound. Any attempt to move in this direction could be more challenging if the government isn't able to demonstrate that there is no ulterior motive. In 2019, the BoE governor Carney indicated the BoE would be undertaking a review to discuss policy constraints associated with the next crisis, including a debate about the inflation target. Carney's preference was that no change was necessary as the BoE already had enough flexibility around its existing target. That policy review has been quietly dropped since the pandemic, even though it leaves many questions unanswered. But in any case only the government would have the authority to sanction a mandate change, and any future move here will be closely scrutinized.

From the BoE's perspective, current Governor Bailey has expressed a preference for starting to reduce the BoE's balance sheet ahead of the first rate hike, and the BoE is currently reviewing its balance sheet guidance. One stated motivation for this is that it would be prudent and free up more scope for the balance sheet to be used actively again in the next downturn. Any such unwind from the BoE would likely be very slow, but a switch in normalization strategy would help to reduce some of the political conflict described above.

Economic Research Note

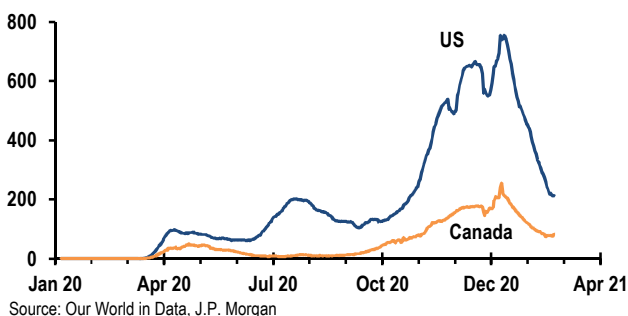
Canada still recovering from COVID

- **The COVID-19-induced economic contraction was somewhat deeper in Canada than in the US**
- **The vaccination effort is also proceeding more slowly, and the fiscal policy response has not been as strong**
- **Our forecast looks for a Canadian economic rebound that is quite rapid by normal standards, but lags the US**
- **Still, the Phillips curve has remained steeper in Canada than the US, so the BoC may move faster than the Fed**
- **We look for tapering of asset purchases by the end of 2021 and the policy rate on hold until 2023**

Canada's record in handling COVID-19 has been mixed. On the one hand, Canada succeeded in holding per capita cases and deaths below US levels (Figure 1). But this success came at the cost of a somewhat deeper economic downturn (Figure 2). Canada's vaccine rollout is also proceeding more slowly (Figure 3), and Canada does not appear to be considering additional fiscal support on the same scale as we expect in the US. As a result, our forecast looks for the Canadian economic rebound to continue lagging the US, even as it proceeds at a rapid rate compared to past recoveries (Figure 2). We look for 5.2% real GDP growth in 2021 (4Q/4Q) and 2.8% in 2022.

Figure 1: US and Canada new COVID-19 cases

New cases per million population, 7-day avg.



The Canadian debate about inflation and the appropriate stance of monetary policy will sound quite familiar to those following the US debate. Like many DM economies, Canada has struggled with inflation running below its target in recent years, although the gap was closing more clearly in Canada during the tight labor markets pre-COVID. During the pandemic, the Bank of Canada has adopted a dovish stance much like the Fed's, and, in fact, was first to pledge to keep short-term interest rates at the zero lower bound until "the 2 percent

inflation target is sustainably achieved," in the Bank's words. The Bank's forecasts currently foresee this occurring in 2023. The Bank has also pledged to continue its ongoing asset purchases of at least C\$4 billion per week "until the recovery is well underway." Our forecasts look for the Bank to begin tapering its asset purchases in the second half 2021, but to keep the policy rate at the lower bound through the end of our forecast horizon in 2022.

Figure 2: Real GDP level and forecast

index, 4Q19 = 100

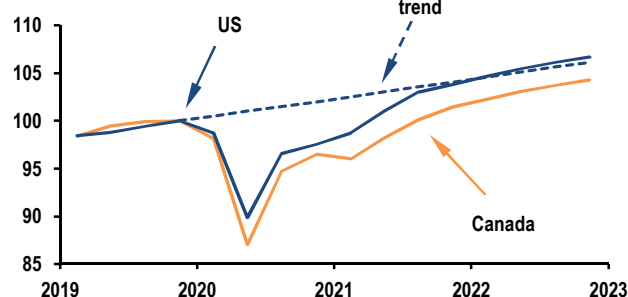
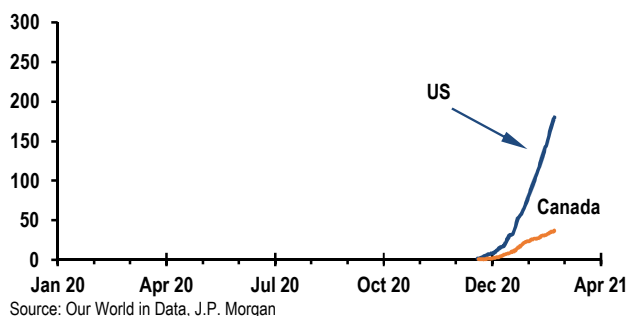


Figure 3: US and Canada COVID-19 vaccinations

Cumulative vaccinations per thousand population, 7-day avg.



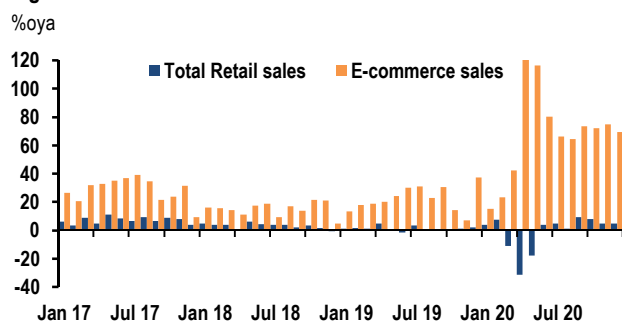
Consumers come back big

With the onset of the pandemic last spring, provincial COVID containment measures forced consumers to cut back dramatically on services spending and to shift away from physical stores for their goods shopping. While consumer spending rebounded sharply following its initial plunge in 1H20, we estimate that household consumption was still around 2% below its pre-COVID level in 4Q20, and the saving rate remained unusually high near 3Q's 15%, significantly higher than the long-run average.

Using non-business real services spending from the monthly GDP accounts as a proxy, real services consumption in November was more than 2% below its February level while goods spending was slightly above its pre-virus trend by November. Goods spending was uneven across sectors, however. Real spending at clothing stores declined 11% from pre-

COVID levels, similar to the experience in the U.S., while other categories accelerated notably, including grocery stores, building material stores, and electronics stores. Auto sales remain below their pre-pandemic pace. Digital shopping served as the buffer, evidenced by tremendous growth in retail e-commerce. Since last March, e-commerce retail sales are up more than 60% on our seasonal adjustment compared to the pre-pandemic trend, and now account for 8% of total retail sales compared with 4% in the fourth quarter of 2019 (Figure 4). The shift toward e-commerce is likely to persist after the pandemic.

Figure 4: Retail sales



Source: Statistics Canada; J.P. Morgan

As new infections began to surge again during the second wave of the pandemic, provincial authorities took steps to renew social distancing measures. The tightest and most expansive restrictions began at the end of December and are set to hold down consumption in the first quarter. We expect a 2.5%q/q, or decline.

Consumers are well-situated for a bounce in consumption. Households can expect another tranche of the Canada Child benefit in 2021, up to C\$1,200 for each child under the age of 6 on a quarterly basis—an almost 20% increase. And consumer confidence is back to pre-pandemic levels. Along with continued unprecedented levels of government support, the healing labor market has led to a recovery in total labor income—hours worked multiplied by average hourly earnings—and one that should support solid consumer spending (Figure 5). We expect consumer spending to re-accelerate as a larger percentage of the population becomes inoculated against COVID-19 and provincial restrictions continue to ease. The reopening of schools and retail shops for onsite shopping and even a partial reopening of services should support a rapid rebound in consumer spending in 2Q21, consistent with the experience in 3Q20.

Figure 5: Payroll proxy, hours worked times hourly earnings



Source: Statistics Canada; J.P. Morgan

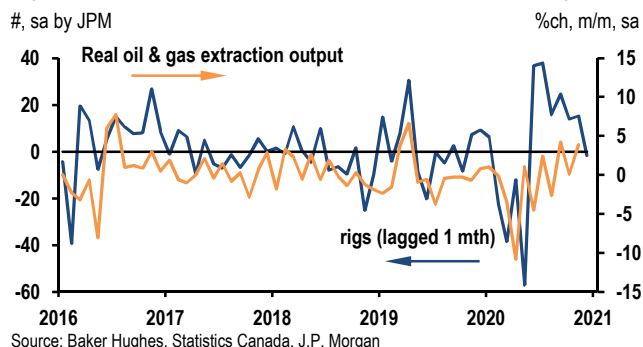
There are potential headwinds, however. The scarring of successive waves of the pandemic has left many consumers apprehensive. Interest-sensitive sectors like housing and autos loans have already rebounded. The pent-up demand in those sectors is likely to taper off later this year leading to more muted consumption growth. Thousands of people are still out of work and finances remain stretched. Some savings will be allocated to pay down debt still in forbearance and other bills that have been put off. Among the insured mortgages that were outstanding at the end of March, a little over 17% had exercised the government payment deferral option by early summer. By October, the percentage had dropped but was still high at 7.2%. Still, we look for robust spending gains of 4.8% in 2021 overall (4Q/4Q).

Build back better

Nonresidential fixed investment plunged at a 27.9% average annualized pace in 1H20, but rebounded powerfully in the third quarter (25.8%) driven by a surge in machinery and equipment spending. Our two proxies for the growth of business equipment spending are volume shipments of durable goods and volume imports of machinery and equipment, and both are tracking solid increases in 4Q. Taken together we estimate that equipment spending grew moderately in 4Q; we project a 5%, or gain in equipment spending and then a stall in 1Q21 (0%).

On nonresidential construction we take our cue from non-residential permits. Overall, the value of non-residential construction permits posted a large decline last quarter, down 17.0% to reach the lowest value in the past four years. All components were down, with the commercial component setting a record drop-off of 21.2% and reaching its lowest level since 2017. A decline in engineering structures mostly can be pinned to the drop in oil prices (Figure 6).

Figure 6: Real extraction output in the GDP accounts and rig count



We expect capital spending will continue to rebound through 2021. The Bank of Canada's low policy rate, forward guidance, and quantitative easing (QE) program will keep business financing conditions favorable, and firming upstream prices will support profits. Inventories are still looking relatively lean at the start of 2021 and we expect continued strong growth in digitalization, cloud infrastructure, and online services will lead to steady growth in intellectual property investment.

Business sentiment on investment suggests there is reason to be hopeful. In the latest Bank of Canada Business Outlook Survey from late November, firms were looking beyond the second wave of the COVID-19 virus and pondering their plans beyond the pandemic. Firms had a more positive sales outlook for the next 12 months with the balance of opinion on future sales at the highest level since 2009. The balance of opinion on spending moved up in firms across all provinces. Machinery and equipment spending plans were more upbeat and spread across firms shielded from the most negative effects of the pandemic as well as recovering businesses expecting conditions would eventually return to normal.

The energy sector may prove an exception to the positive capex outlook, however. The sector began 2020 under a cloud of uncertainty pinned to pipeline gridlock and mandated limits on oil production. And then the pandemic and slump in oil prices hit the energy sector hard. With the ongoing restructuring in the oil sector, we don't see a genuine revival in energy sector investment on the horizon (Figure 7).

Figure 7: Capital expenditures, oil and gas extraction



Our house is a very fine house

Pent-up demand, low mortgage rates, and a pandemic-driven desire for homes with more amenities all point to a strong outlook for residential investment. Lockdown measures pummeled housing market activity last spring with existing home sales declining by over 33% between the first and second quarter of 2020. New listings and new construction were also hard-hit. With economic and labor market conditions measurably improved by the third quarter, demand for existing homes and single-family new construction increased tremendously. The spirited revival in housing activity more than reversed the springtime declines—real residential investment surged 30%/q, or in 3Q after falling 15%/q in 2Q. Thus far, the upswing has shown little sign of waning. In the last two months existing home sales ran at a seasonally adjusted annualized pace well above 700,000 units, the first time on record that the monthly pace topped that number (Figure 8). Housing starts and permits have already exceeded their pre-virus levels.

Figure 8: Housing market

6-month moving average, thousand units, saar, both scales



New listings of existing homes have not kept pace with demand, putting upward pressure on house prices. Price growth also reflects a sudden shift in homebuyers' preferences toward larger homes to accommodate remote work. A run-up in the cost for lumber has also driven up the price of new construc-

tion and renovation projects. Since heated price growth largely can be pinned to a shift in the composition of sales and temporary supply bottlenecks rather than underlying fundamental economic conditions we don't believe it will be sustained.

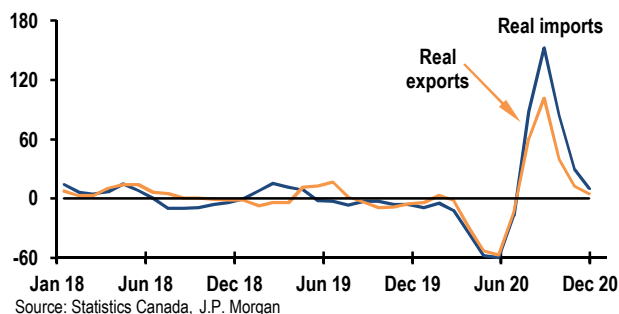
While the boomiest growth for the housing market is now likely in the past, forward-looking indicators like residential permits continue to climb, which suggests activity in the pipeline. Nevertheless we expect the market will cool once the pent-up demand is satisfied. We forecast that real residential investment will increase 19% in 2021 after closing out 2020 with a projected 102%, saar average gain during the second half of the year. We expect the cost of borrowing will continue to hover at all-time lows given the Bank of Canada has signaled low-for-long interest rates.

Activity south of the border will rub off on exports

Fallout from the pandemic hit export performance especially hard in 1H20. The collapse in oil demand pummeled energy exports, while lockdowns and supply constraints sent auto exports reeling. Trade in services also suffered as travel declined to a trickle. Real goods exports and imports bounced back in the third quarter as lockdowns eased and consumption boomed. Trade growth moderated significantly in 4Q but remained positive (Figure 9). Real merchandise exports are still down over 7%/y in 2020 while real imports are down over 8%/y. The positive story is that Canada's overall terms of trade recovered to the pre-pandemic level by year-end, helped by the strength in the currency and the rebound in oil prices. We believe the generally bullish outlook for oil prices and robust growth in the US economy will spur export performance this year. Services trade is also likely to recover somewhat but we don't expect the travel sector to return to pre-pandemic levels by year-end 2021.

Figure 9: Merchandise trade flows

%ch, 3m/3m, saar, chained 2012 C\$

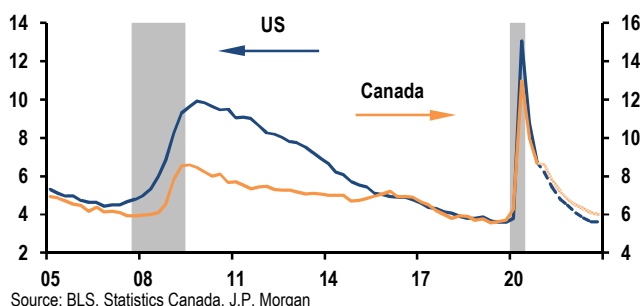


Tight labor market to tug at inflation

All in all, we look for robust 5.2% growth in 2021 (4Q/4Q), which should be enough to produce rapid job growth and labor market tightening. Our forecast looks for the Canadian unemployment rate to return to 6% by the end of our forecast horizon in 2022, just a touch above the 5.4% historic low seen before COVID (Figure 10).

Figure 10: Unemployment rates and JPM forecasts

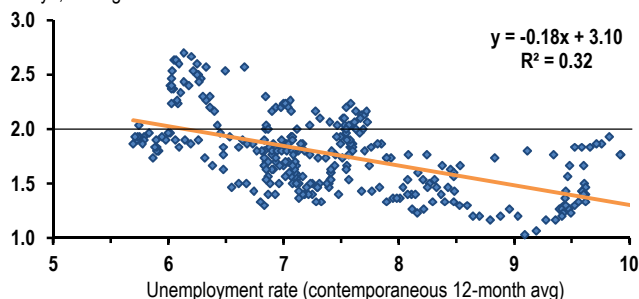
%qtr avg, both scales



Although the economy has a long way to go from here to achieve this labor market forecast, we are somewhat more confident that a tight labor market will produce inflationary pressure in Canada than in the US, as the Canadian Phillips curve has remained steeper than the US equivalent (Figure 11). The Bank of Canada's preferred core inflation measures have risen more clearly near 2% during tight labor markets than the Fed's preferred core PCE inflation metric in the US.

Figure 11: Canada Core CPI Phillips curve, 1995 to present

%oya, average of Bank of Canada three core inflation measures



Thus, despite the more sluggish GDP recovery that we project in Canada, it is quite possible that inflation will firm a bit sooner and induce the Bank of Canada to move somewhat more quickly than the Fed in the coming years. The Bank of Canada's forecasts currently suggest that rate hikes will begin in 2023, while we pencil in 2024 for the Fed. Neither central bank has provided much detail on their thinking about the timing of asset purchase tapering, but we look for the Bank of Canada to begin tapering its asset purchases in the latter half of 2021.

Economic Research Note

Turkey: Better external balances to help reserve buildup

- Improving external balances and stronger capital inflows could result in a virtuous cycle
- Tighter financial conditions, normalized gold demand, and stronger tourism will reduce the current account deficit sharply
- We expect CAD to narrow to US\$20 billion (2.4% of GDP) in 2021 from US\$36.7 billion last year
- Strong investor sentiment should fuel continued portfolio inflows and bank/corporate borrowing abroad

The appointment of credible and experienced people to key government posts and the CBRT's tightening and policy simplification have led to an abrupt improvement in investor sentiment on Turkey. For this trend to be sustained and eventually to lead to a virtuous cycle, two things are needed, in our view: 1) structural reforms to support prudent policies and 2) significant gains in price and financial stability. While we have yet to see any progress on structural reform, we are confident that there will be progress on stability. Regarding financial stability, import compression led by weaker loan growth, normalized gold imports, and stronger tourism likely will result in a significant narrowing of the current account deficit. Lower current account outflows along with strong portfolio inflows and some de-dollarization by local investors would result in a recovery of the CBRT's official reserves and this in turn could lead to further improvement in sentiment, further capital inflows, and de-dollarization; in short, a virtuous cycle. Higher commodity prices, geopolitical factors, and premature policy easing stand out as the key risks in this scenario.

Weakness in travel and transportation to reverse

Between December 2019 and December 2020, Turkey's current account balance worsened swiftly and persistently to a deficit of US\$36.7 billion (5.2% of GDP) from a surplus of US\$6.8 billion (0.9% of GDP, Figure 1). The direct impact of this widening was higher external borrowing needs and hence stronger pressure on the lira. The widening of the deficit and the resulting fall in CBRT reserves also weakened sentiment and aggravated pressure on the lira by prompting portfolio outflows and extra FX demand by local investors. We need to find the factors responsible for this widening to forecast Turkey's external balances for 2021. Figure 1 strongly implies that higher gold imports and weaker travel and transportation revenues have been the main factors. Excluding those, the

worsening has been much milder (from a deficit of 5.0% of GDP to 5.4%). Table 1 provides a more comprehensive picture.

Figure 1: Current account balance, 12-month trailing, nsa
% of GDP

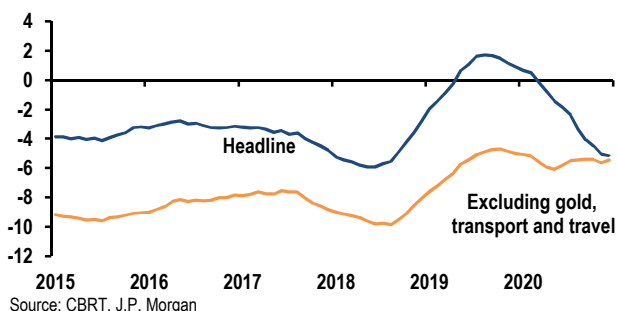


Table 1: Factors behind the worsening in the current account balance
US\$ billion, 12-month trailing

	2019	2020	Change
Current account balance	6.8	-36.7	-43.5
Foreign trade balance	-16.8	-37.9	-21.1
Exports of goods	182.2	168.2	-14.0
Imports of goods	199.0	206.1	7.1
Energy	41.7	28.9	-12.8
Gold	11.3	25.2	13.9
Other	146.0	152.0	6.0
Incomes balance	35.5	9.6	-25.9
Tourism	25.7	9.2	-16.5
Transportation	14.6	5.7	-8.9
Other	-4.8	-5.3	-0.5
Other	-12.0	-8.5	3.5

Source: CBRT

It was not surprising to see a pandemic-related plunge in tourism and transportation revenues. These two factors were responsible for more than half of the current account worsening last year. Indeed, the situation would have been much worse if part of Turkey's tourism revenues had not come from the family visits of Turkish workers in Europe and ethnic Turks in the Balkans. Similarly, sharply weaker global demand and bottlenecks in transportation led to a US\$14 billion drop in total merchandise exports. With the recovery in global growth and hopefully an easing of travel and transportation restrictions, we expect a reversal of this trend this year. Vaccinations are going relatively fast both in Turkey and in countries Turkey mainly attracts tourists from (Europe and the Middle East). We expect Turkey's net tourism revenues to increase to US\$17 billion in 2021. This will still be significantly lower than historical norms and hence can be considered a conservative projection. Furthermore, J.P. Morgan expects PPP-weighted global GDP growth to recover to 6.8% in 2021 from a 3.8% contraction last year. This recovery will almost certainly lead to a sharp recovery in merchandise exports.

Also supportive will be lira stability. The lira has almost consistently lost value and this has become more evident in the last five years (Figure 2). However, Turkish exporters have not exploited the resulting improvement in price competitiveness. In fact, although Turkey's share in global exports has risen consistently since the start of the millennium, rapid growth occurred when the lira was relatively stable and Turkey gained competitiveness through productivity gains in the early years of the 21st century (Figure 3). The relative stagnation in recent years, in our view, mainly was due to excessive volatility in the currency market and the resulting difficulties in pricing. With a more stable lira, exporters could finally benefit from the price competitiveness gains resulting from the cumulative lira depreciation seen in recent years.

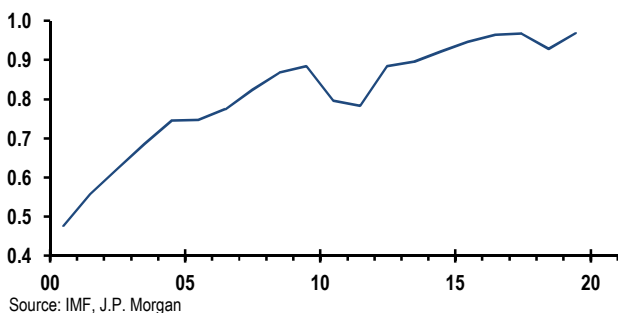
Figure 2: Real broad effective exchange rate

Index, 2010=100



Figure 3: Share of Turkey in global exports

% of total

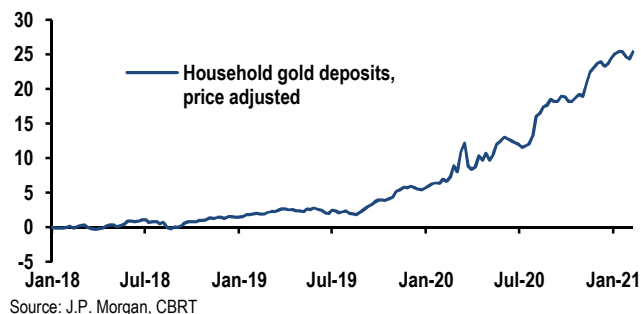


Gold imports and credit impulse behind import strength

The two other factors responsible for last year's CAD widening—i.e., sharply higher gold imports and the resilience of other imports—were idiosyncratic. The erosion in policy credibility led to a substantial change in the portfolio preferences of local investors. This change mainly took the form of sharply higher investments in gold. In fact, the gold deposits of local investors in the local banking system increased by US\$18 billion in 2020 (Figure 4).

Figure 4: Cumulative change in household gold deposits

US\$ bn

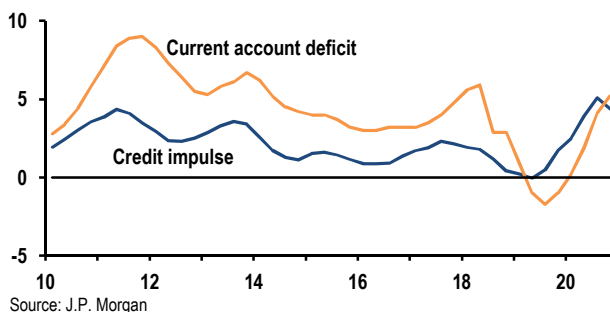


We presume there was an increase in gold savings under the pillow as well. This looks like the main reason for the surge in gold imports. With stronger policy credibility, local demand for gold has subsided in recent weeks. Continued prudence in policy implementation along with high TRY interest rates will likely encourage local investors to de-dollarize further and shift to the lira. This, in turn, should push gold imports back to their normal annual level of US\$10 billion.

A final interesting part of last year's external balances narrative is the resilience of imports. Despite weak GDP growth, imports rose 7%oya in 2020, compared with the 14%oya plunge in exports. This resilience, in our view, mainly was due to the government-engineered credit impulse in the first half of the year. Figure 5 shows the strong correlation between the credit impulse (defined as the annual increase in consumer loans and individual credit card balances as a percentage of GDP) and the CAD. Last year's impulse was by far the largest in recent history and this contributed significantly to the widening in the CAD. With tighter financial conditions, loan growth has nearly stalled in recent weeks. We expect this tightness in financial conditions to continue and keep annual loan growth below 10%, helping to reduce the CAD.

Figure 5: Consumer loans and external balances

% of GDP



All in all, we expect Turkey's CAD to narrow to US\$20 billion (2.4 % of GDP) in 2021 from US\$36.7 billion (5.2% of GDP) last year. This projections reflects our assessment that 1) exports will rise 7%oya on the back of stronger global growth and slightly better price competitiveness; 2) net tourism revenues will recover partly to US\$17 billion from US\$9 billion; 3) gold imports will normalize to US\$15 billion from US\$25 billion; 4) oil imports will rise 20% on the back of higher prices; and 5) other imports will grow 6%oya.

We expect the CBRT to keep rates on hold until September. If policy remains tighter for longer, a much smaller deficit would be possible. Similarly, a stronger recovery in global demand and earlier easing of travel restrictions would help Turkey's external balances. The main downside risk to our scenario is a steeper-than-expected rise in commodity prices. As a large commodity importer, the impact of this on Turkey could be much larger than on other countries. Another major risk is a premature easing of policies. Finally, any rise in geopolitical risks could result in anxiety among local investors, delaying the normalization in gold imports.

Capital flows also to be supportive

The capital account also worsened significantly in 2020 and, as with the current account, we expect a reversal this year driven by prudent policies and stronger investor appetite. Turkey's total financing need in 2020 was US\$40 billion and despite the US\$10 billion coming from the Qatar Central Bank to the CBRT, total capital flows stayed at US\$8.2 billion, resulting in official reserves being depleted by US\$32 billion last year (Table 2).

Table 2: Current account financing

US\$ billion

	2018	2019	2020	2021F
Current account balance	-21.7	6.8	-36.7	-20.0
Net errors and omissions	10.8	-5.5	-3.3	0.0
Total financing need	10.9	-1.3	40.0	20.0
Capital movements	0.5	5.0	8.2	36.7
FDI	9.2	6.3	4.6	5.5
Portfolio investments	-3.1	-1.4	-5.5	18.2
Eurobond issuance	3.9	6.8	4.6	3.2
Purchases by foreigners	-3.8	-3.5	-9.9	15.0
Equity	-1.1	0.4	-4.3	3.0
Bonds	-0.9	-3.1	-5.0	7.0
Banks	-1.0	-1.0	0.2	3.5
Corporates	-0.8	0.2	-0.8	1.5
Domestic purchases abroad	3.2	4.7	0.2	0.0
Loans	-2.2	-3.5	-9.6	11.0
Central government	-0.8	-0.9	-0.4	0.3
Banks	-15.1	-11.3	-5.1	3.4
Nonbanks	13.7	8.8	-4.2	7.4
Deposits	-0.4	4.5	19.8	5.0
Other	-3.0	-0.9	-1.1	-3.0
Reserve accumulation	-10.4	6.3	-31.9	16.8

Source: CBRT, J.P. Morgan

The public sector was the only net borrower offshore in 2020. Apart from the US\$10 billion from Qatar, US\$4.6 billion in net eurobond issuance also helped to prevent an even deeper reserve depletion. Portfolio outflows from nonresidents totaled US\$9.9 billion. Furthermore, as deleveraging continued, both banks and nonbanks were net payers in the loan market. The other major inflow was in the deposits of local banks, reflecting relatively high interest rates at home. Finally, net FDI inflows contributed US\$4.6 billion, but this was the lowest annual inflow in 16 years.

With significantly higher interest rates and much stronger policy credibility, we expect a totally different picture this year. It is too early to expect a meaningful pickup in FDI inflows. Investors would first have to be confident that prudent and market-oriented policies based on rule of law would persist before making FDI investments. Also necessary, in our view, is some progress on structural reforms. Hence, strong FDI inflows are quite unlikely in the short run. Portfolio flows could easily strengthen, though. We see a total of US\$15 billion in portfolio inflows this year. Compared to previous years of strong investor sentiment, this is not an aggressive assessment. Turkey attracted US\$33 billion in portfolio inflows in 2012, US\$17 billion in 2013 and 2014, and US\$18 billion in 2017. Also important is the low exposure of international investors in Turkish capital markets. For instance, the share of nonresidents in the local government paper market is currently 5.4%. Foreign participation was around 20% for most of the time between 2013 and 2018, a measure of the upside potential in portfolio inflows. A rise in core rates is surely a risk but given how wide Turkey's spreads are, we would not expect Turkey to be much affected by this.

Deleveraging supports financial stability

In the loan market, Turkish companies have been deleveraging for three years and this trend strengthened last year. The deleveraging was partly voluntary and partly imposed by market conditions. The deleveraging is clear in the FX assets and liabilities of the nonbank sector in Table 3. The short FX position of the nonbank sector narrowed to US\$158 billion from US\$218 billion in the 1.5 months to November 2020. This was achieved by an increase in FX deposits (which explains part of the dollarization) and by a drop in FX loans to the banking sector. Corporates closed US\$35.6 billion of FX-linked debt they borrowed from the local banking system. Seeing the drop in their FX assets, banks responded by closing their FX borrowing. In fact, Table 2 shows a banking sector net debt repayment of a similar magnitude over the last three years. The deleveraging in recent years surely reduces risks to financial stability. Importantly, the short-term FX assets of the non-banks currently exceed their short-term FX liabilities by US\$26 billion, up from just US\$2.8 billion in mid-2018. This shift implies that rollover risks are much lower now.

Table 3: FX assets and liabilities of the nonbank sector

US\$ billion

	2018/6	2020/11	Change
Assets			
Deposits	76.1	96.1	20.0
Securities	0.3	1.5	1.2
Export Receivables	18.4	20.2	1.8
Direct Investments abroad	18.6	20.8	2.2
Total	113.4	138.6	25.2
Liabilities			
Domestic loans	181.1	145.5	-35.6
External loans	102.9	98.5	-4.4
Import payables	47.4	53.0	5.6
Total	331.4	297.0	-34.4
Net FX position	-218.0	-158.4	59.6
ST net FX position	2.8	26.0	23.2

Source: Undersecretariat of Treasury, J.P. Morgan

With a significant change in market conditions, we would expect a reversal in credit flows as well. Two factors should support this reversal: First, more prudent and rule-based economic policy making has already led to a significant improvement in lenders' perception of Turkey and Turkish companies. Second, with high real rates at home and a stable currency, Turkish companies would prefer to increase their external borrowing. Given the much more balanced initial conditions and the heightened caution of Turkish companies, we expect this new phase of leveraging to be much smoother than before.

As a result of these favorable changes, we expect official reserves to increase by US\$16.8 billion this year. If the improvement in external balances is accompanied by some reverse currency substitution by local investors, then the CBRT will be able to increase its reserves through FX purchase auctions as well. As bringing inflation down remains the main policy priority, the CBRT would welcome currency strength in the near term and we expect these auctions only in the second half of the year.

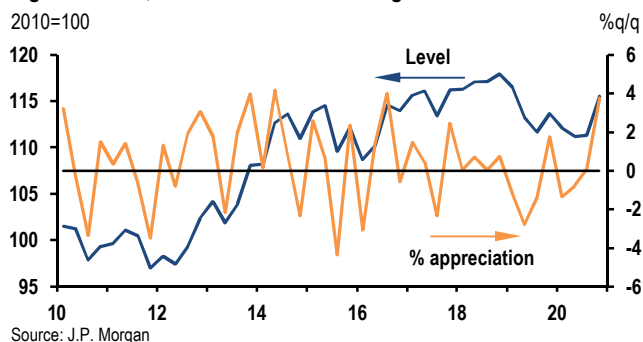
Economic Research Note

Korea: FX passthrough may not be a hurdle for BoK action

- Sensitivity of inflation and exports growth to FX moves has waned in last decade
- BoK's track record suggests that FX appreciation does not preclude hikes
- Instead of FX, BoK's focus is on growth, inflation, and household leverage
- We expect BoK to hike in 1Q22

In 4Q20 the Korean won (KRW) appreciated 3.8% in nominal trade-weighted (NEER) terms, in part reflecting Korea's out-performance in merchandise goods exports and real GDP growth compared to trading partners (Figure 1). We had highlighted the risk that the Bank of Korea's monetary policy communication might turn hawkish late this year due to a closing output gap amid a resilient macroeconomic backdrop. But currency appreciation may raise the bar for monetary policy normalization, possibly through a spillover to domestic disinflation and a drag on real exports growth, given that we forecast about 5.3% further KRW appreciation vs. USD by end-2021 amid a 1.7% fall in the USD index. However, this note shows that FX passthrough to domestic prices and exports growth has waned in recent years, and historically the BoK's actions have not been affected much by currency moves. In all, potential spillover from (expected) currency appreciation should not be a hurdle for possible BoK rate hikes next year, but growth, inflation and household leverage issues will remain key to upcoming decisions.

Figure 1: KRW, nominal effective exchange rate



FX passthrough to consumer inflation has decreased

A simple regression analysis shows a 6.8%-pt passthrough from NEER to consumer inflation since 2000, i.e., a 10% NEER appreciation would be associated with a 0.68%-pt drop

in consumer inflation (Table 1). We postulate two-stage FX-to-consumer price spillover path, as i) NEER affects imported prices in KRW terms (90.8%-pt passthrough), then ii) imported prices affect CPI (7.5%-pts).

Table 1: NEER spillover to CPI

%pt impact	Whole sample	2000-07	2010-19
NEER to imported prices ¹⁾	90.8	72.8	88.0
Imported prices to CPI ²⁾	7.5	9.0	5.1
NEER to CPI ³⁾	6.8	6.6	4.5

Source: BoK, NSO, and J.P. Morgan estimates

* Regression results of monthly log return of variables, up to 2 months' lag

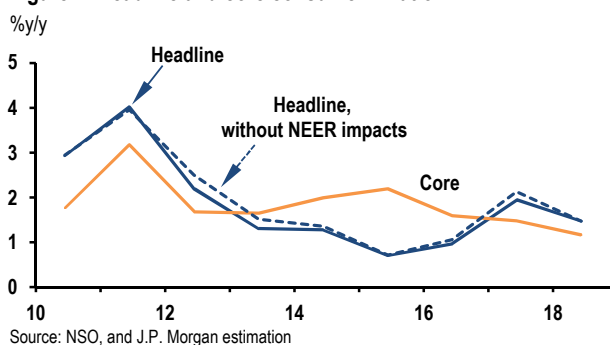
1) Sum of regression coefficients of NEER, in a regression equation of imported prices (in KRW) on NEER and imported prices in contract currencies.

2) Sum of regression coefficients of imported prices in KRW, in a regression equation of CPI on imported prices in KRW and cyclical indicator.

3) Multiplication of 1) and 2) effects

Interestingly, we estimate overall price passthrough decreased to 4.5%-pts in the post-Global Financial Crisis (GFC) sample. The NEER's impacts on imported prices remained elevated in the post-GFC sample, yet imported prices' impact on final consumer prices decreased in the last decade. Using the estimated passthrough, the 11.4% NEER appreciation during 2012-13 (the main NEER appreciation episode since the GFC) would have dragged down consumer inflation by 0.5%-pt, while headline inflation has slowed from 4.0%/y in 2011 to 2.2% in 2012 and 1.3% in 2013. Thus the FX spillover impact on disinflation during 2012-13 was modest, while the other forces such as the downturn in domestic demand and global oil prices (in foreign currency term) dominated (Figure 2).

Figure 2: Headline and core consumer inflation



Exports' sensitivity to FX value has waned

If a nominal FX appreciation is not fully offset by changes in relative prices (domestic vs. foreign prices), then real currency appreciation may drag down exports growth through relative price effects. Yet again, we estimate the sensitivity of Korea's real exports to the real effective exchange rate (REER) has declined in recent years.

Table 2: Real exports response to REER
 estimated coefficient

	Whole sample	1980-96	1999-2007	2010-19
REER	-0.86***	-1.46*	-0.33	-0.03
REER(t-1)	-0.53	-2.05**	-0.84	0.18
Global growth	3.45***	3.02**	2.36	-1.48
Global growth(t-1)	-0.59	-1.52	3.81*	2.74

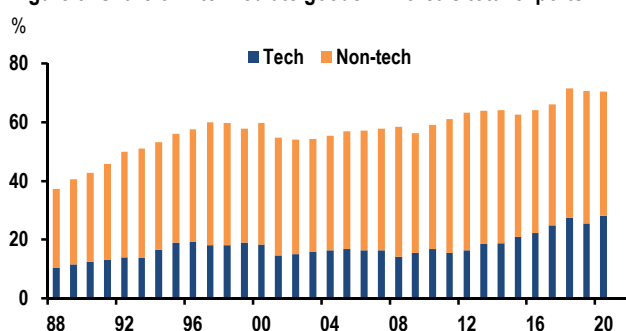
Source: BoK, and J.P. Morgan estimates

*** denotes significance under 1% error, ** under 5%, and * under 10%

Table 2 shows regression analysis results of quarterly real exports growth, explained by current and 1-quarter-lagged REER appreciation and global real GDP growth (to control for the impact of foreign demand conditions). In the whole sample from 1980, we estimate REER appreciation dragged down real exports growth in the concurrent quarters (0.86%-pt for 1% appreciation). Dividing the sample into the 1980 to Asian Financial Crisis (AFC) period, post-AFC to GFC, and post-GFC to pre-COVID-19, there were notable changes in the sensitivity. The REER impact on real exports was greatest in the 1980-96 subsample, and insignificant in the later samples.

One explanation for the diminished exports response to the REER is a structural change in Korean exports: moving up in the global trade value chain. That is, the share of intermediate goods in Korean exports has increased steadily from 37% in 1988 to 71% in 2020, in both tech and non-tech goods (Figure 3), including semiconductors, electronic parts, battery cells, and petrochemical materials, implying that relative prices became less relevant for Korean exports performance as export demand for such high-value intermediate goods tend to be less sensitive to prices than the demand for lower-value-added products.

Figure 3: Share of intermediate goods in Korea's total exports



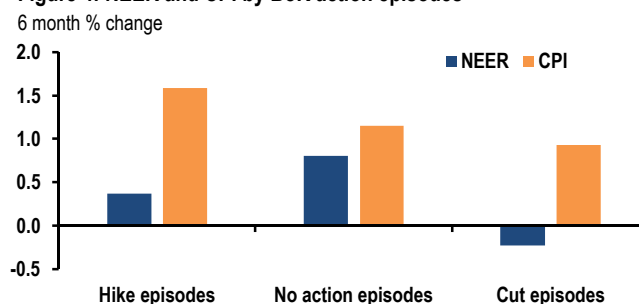
Source: MoTIE, and J.P. Morgan

Currency value may not be a major obstacle to BoK hike

Tightening financial conditions through FX appreciation is one of the transmission channels of monetary policy tightening, but preemptive appreciation through market expectations

(or for other reasons) may raise the bar for rate hikes. That said, in the Korean context, we have shown that FX spillover to domestic inflation and real exports has decreased in the last decade, and Figure 4 illustrates that the BoK's reactions have not been tightly correlated with NEER changes prior to policy rate decisions. That is, hikes unsurprisingly were associated with higher consumer inflation, yet, taking the average six-month % NEER change prior to each action, the KRW NEER appreciated on average prior to rate increases. This correlation reflects the endogeneity of hikes and the macroeconomic cycle, as higher inflation and currency appreciation typically are associated with a positive macroeconomic backdrop (i.e., a positive output gap). If the macroeconomic backdrop justified a rate hike, then the BoK historically hiked even though the currency appreciated.

Figure 4: NEER and CPI by BoK action episodes



Source: BoK, NSO, and J.P. Morgan

* Average of changes prior to BoK action events since 2000

In all, in determining the path of monetary policy normalization in 2021-22, we think the BoK's primary consideration will not be FX moves. Instead, as reiterated by post-MPC communications and MPC minutes, policy decisions primarily will try to balance the need for accommodation from a negative output gap and subdued inflation with stabilization needs arising from household leverage. Against this backdrop, we expect the output gap to close in 2022 and core inflation to firm gradually, and think that policy decisions will put more weight on the financial imbalance issue from household leverage. Financial conditions may tighten modestly from NEER appreciation this year, but we expect FX wouldn't be an obstacle to a policy direction change. While the MPC's February communication confirmed that the BoK is not ready to hike yet as it is not confident of a sharp recovery this year, we see greater upside risk to its outlook and changed our policy call this week, expecting the next move to be a hike in 1Q22 followed by another in 3Q22.

United States

- **December stimulus bill led to January surge in income and jump in consumer spending**
- **Core capital goods data carry solid momentum into early 2021**
- **PCE price trends stay modest and Fedspeak stays dovish**
- **We look for 200,000 February increase in nonfarm employment with unemployment rate unchanged**

Our forecast anticipates robust growth in 2021 following the weak end to 2020, and the 2021 data generally have been off to a strong start. This recent pickup in activity clearly looks related to the fiscal supports from the stimulus package passed late in December and the economy also is likely benefiting from recent declines in new COVID-19 cases and vaccine rollouts. Most importantly, real consumer spending jumped 2.0% in January, a month when government transfers led to a 10.0% surge in nominal income. It also looks like business equipment investment carried solid momentum into early this year, with strong trends for key series related to core capital goods orders and shipments. Some housing indicators have cooled lately, but activity in the housing market still looks strong.

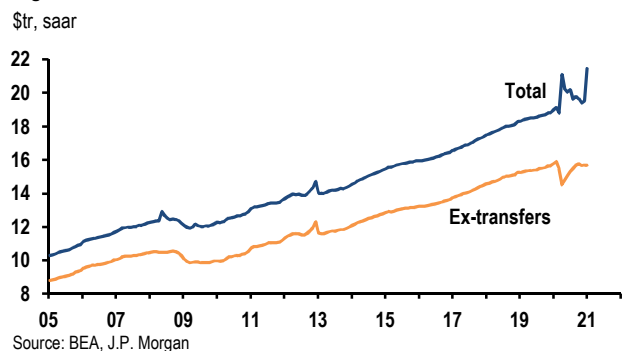
While the economy appears to be picking up some steam, we think growth is really set to get going in the middle of this year. This view is based in part on the assumption that another stimulus package is passed, with another [\\$1.7tn of fiscal stimulus](#) built into our baseline forecast. We still believe that the full \$1.9tn spending package promoted by President Biden is on the high end of possible outcomes, and consistent with this view, it appears that parliamentary issues will prohibit the proposed increase in the minimum wage from being included in the Senate's budget reconciliation process. While we feel comfortable with our assumptions, the exact timing, size, and composition of a potential future stimulus bill is unknown.

The broad underlying inflation trends remain modest even though there has been clear firming since the lows seen early in the pandemic. As of January, the headline and core PCE price deflators were both up 1.5%oia. Modest inflation allows the Fed to keep policy very accommodative even with expectations for strong growth and tightening in the labor market. The Fedspeak from the past week (including testimony from Chair Powell) reinforced recent messaging that the FOMC will keep rates unchanged at the zero lower bound for a while.

More income, more spending

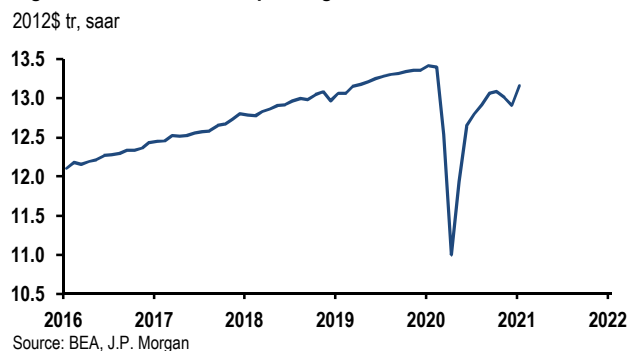
Households received a massive influx of income in January, primarily as a result of the stimulus package that was passed late in December. Total income jumped 10.0% in January with a surge in transfer receipts more than accounting for the total increase (Figure 1). Most importantly, stimulus checks accounted for about \$1.7tn (or about 8%) of income in January and the supplement to UI payments authorized as part of the December package accounted for about \$300bn (dollar figures reported as annualized rates).

Figure 1: Personal income



Consumer spending tapered off late last year in part due to surging new COVID-19 cases and on the onset of colder weather. But the rush of income in January looks to have been enough to reinvigorate consumers to some degree. Real consumption jumped 2.0% in January (Figure 2) and with the saving rate surging above 20%, consumers likely have more in the tank for spending ahead.

Figure 2: Real consumer spending



Continued labor market improvement should help support consumer spending over time and a drop in initial claims filings in the latest weekly report sent a favorable signal about recent changes in the job market (albeit one from a pretty noisy series). A more important issue for consumer spending in the near term is what happens with any upcoming fiscal deal. We currently think that a future stimulus package will generate strong income growth shortly after its passage through a bump up in stimulus payments as well as some other factors.

While consumers appear to be in good shape to keep spending, the [severe winter weather in Texas and some nearby areas](#) in February looks to have led to a pullback in consumer spending that we think will be temporary. We expect the automaker reports on February auto sales released next week to show a decline in sales during the month due to weather-related issues.

Housing a little softer

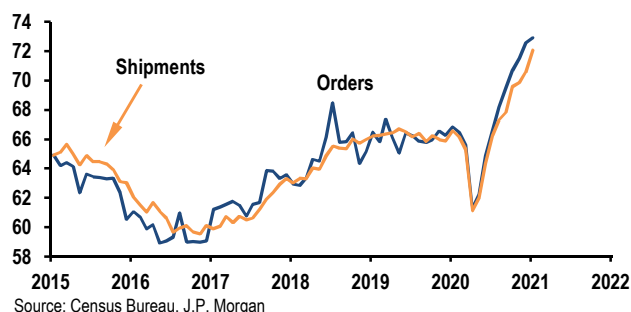
Household income also should support activity in the housing market. That said, it appears that we may have moved past the boomiest period for activity in the market that came when mortgage rates were very low, the pandemic led to increased demand for housing in certain areas, and there was the release of pent-up demand from when activity had been restricted shortly after COVID-19 started spreading. Several housing indicators have moved down from recent peaks, including the data on new home sales and pending existing home sales released this week. But the levels of activity in these measures remain elevated relative to pre-pandemic trends. With housing demand remaining strong, house price appreciation has been robust according to a variety of different measures. In reports this week, the Case-Shiller 20-city composite price index was up about 10%oya in December while the FHFA house price index rose more than 11%oya.

Equipment investment still climbing

On the business side, the January durable goods report showed continued upward momentum for the key series related to core capital goods orders and shipments, including a 2.1% jump in the shipments series in this latest reported month (Figure 3). Equipment spending surged in the second half of last year and we think double-digit growth early in 2021 should be fairly easily attainable given what we can see in some related measures through January.

Figure 3: Core capital goods orders and shipments

\$bn, sa



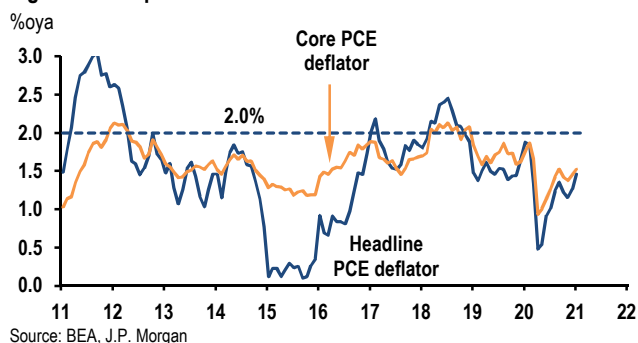
While business investment in equipment has surged during the recovery, investment in nonresidential structures has been very weak. We think softness in this area will continue and

next week's construction report will give us some information about related activity early this year.

Inflation trends modest

The headline and core PCE price indexes both increased 0.3% m/m in January. While these were solid monthly gains, the broader trends in these measures remain modest and both were up just 1.5% oya, about a half point below the FOMC's 2% inflation target (Figure 4).

Figure 4: PCE price indexes



Energy markets currently suggest that increases in energy prices should push up headline inflation readings over the next few months. And we have long been anticipating a jump in over-year-ago inflation rates as these comparisons come up against the very weak inflation data reported in the early stages of the pandemic. But the related strength in inflation should be temporary and we think that the underlying trends will remain modest even as the economy grows rapidly and the labor market tightens. The FOMC appears to have a similar view and has been keeping its communication dovish lately.

Next week's February employment report will give us an updated view on labor market slack as well as signals about growth and wage inflation. We think that employment jumped about 200,000 in February, in part due to favorable virus-related developments in recent weeks. Despite expectations for solid job growth, we think the unemployment rate will hold at 6.3% after rounding.

Data releases and forecasts

Mon Markit manufacturing PMI

Mar 1 Index, sa

9:45am

	Dec	Jan	Flash Feb	Final Feb
Composite ¹	57.1	59.2	58.5	<u>58.5</u>
New orders (30%)	56.5	59.9	57.4	
Output (25%)	58.3	60.5	57.7	
Employment (20%)	52.2	54.7	55.6	
Sup. del. (15%, inv.)	32.5	33.4	26.8	
Stks of purch (10%)	49.7	51.3	47.6	
New export orders	50.7	54.0	53.8	
Backlogs of work	52.3	52.4	54.8	
Output prices	58.6	60.4	61.2	
Input prices	65.3	65.1	73.3	
Stocks of finished goods	48.4	48.1	49.2	
Quantity of purchases	53.4	54.8	53.9	
ISM-weighted composite ²	56.8	58.6	58.3	

1. Weights in parentheses

2. Attributes ISM-composite weights (equal weights) to corresponding PMI series

We look for the Markit manufacturing PMI's headline composite to decline 0.7pt between January and February with the final February figure unrevised relative to the flash reading for the month. We don't see clear signs of a big change in activity in recent weeks that would lead to a large revision in the PMI data.

Mon ISM manufacturing survey

Mar 1 Sa

10:00am

	Nov	Dec	Jan	Feb
Overall index	57.7	60.5	58.7	<u>59.0</u>
Production	62.2	64.7	60.7	
New orders	65.7	67.5	61.1	
Inventories	50.8	51.0	50.8	
Employment	48.3	51.7	52.6	
Supplier deliveries	61.7	67.7	68.2	
Export orders	57.8	57.5	54.9	
Imports	55.1	54.6	56.8	
Prices	65.4	77.6	82.1	

We forecast that the ISM manufacturing survey's headline composite edged up 0.3pt to 59.0 in February. The manufacturing surveys that already have released February data show mixed changes relative to January and we don't expect to see a large change in the national ISM data on net. Like we have seen in many of these other surveys, we expect the ISM survey's composite to come in at a strong level in February, in part due to a high reading on supplier delivery times (which could be related to temporary disruptions associated with the weather and/or supply chain issues).

Construction spending

Mon

Mar 1

10:00am

%m/m, sa

	Oct	Nov	Dec	Jan
Nominal	2.5	1.1	1.0	<u>0.8</u>
Private	2.4	1.5	1.2	<u>0.9</u>
Residential	4.8	3.0	3.1	<u>2.2</u>
Nonresidential	-0.7	-0.6	-1.7	<u>-1.2</u>
Public	2.6	-0.1	0.5	<u>0.6</u>

We believe that construction spending increased 0.8% in January. Spending on private nonresidential construction has been increasing rapidly lately but the pace of growth has cooled somewhat; we look for a continuation of these trends in January with private residential spending up 2.2%. Private nonresidential spending, meanwhile, has been trending lower lately and we forecast another decline for January with spending down 1.2%. Public construction spending has risen in recent months through some ups and downs in the monthly data and we look for another increase in January with spending up 0.6%.

Tue

Mar 2

Motor vehicle sales

Millions, saar

	Nov	Dec	Jan	Feb
Light trucks and autos	15.7	16.2	16.6	<u>15.6</u>
Imports	3.6	3.6	3.8	
Domestics	12.1	12.6	12.8	
Autos	2.9	2.7	2.7	
Light trucks	9.2	9.9	10.1	

We look for light vehicle sales of 15.6mn saar in February based on available industry guidance and we think that this step down in the sales rate is primarily related to severe winter weather in certain parts of the country.

Wed

Mar 3

8:15am

ADP employment

Change from month ago, sa

	Nov	Dec	Jan	Feb
ADP	299	-78	174	
BLS private payroll	359	-204	6	

Last month, the January ADP report indicated that private payrolls increased by 174,000 during the month while the BLS data showed an increase of only 6,000. This overestimation by the ADP data broke the streak of nine straight months in which the ADP data looked weaker than the BLS data (when comparing first prints). And it remains difficult to use the ADP data as a signal for forecasting the BLS employment figures.

Wed **Markit services PMI**
Mar 3 Index, sa
9:45am

	Dec	Jan	Flash Feb	Final Feb
Business activity	54.8	58.3	58.9	<u>59.0</u>
Incoming new business	54.6	55.8	56.9	
Employment	53.4	51.1	50.9	
Business expectations	65.4	73.5	74.2	
Input prices	64.7	66.9	70.3	
Prices charged	56.2	58.3	59.0	
Backlogs of work	51.8	50.8	51.9	

We look for the Markit services PMI's headline activity index to be revised up from 58.9 to 59.0 between the flash and final February reports, with this updated figure 0.7pt above the final January reading. With vaccine rollout continuing and new COVID-19 cases generally trending lower in recent weeks, we think that the service sector will continue to recover with activity picking up over time.

Wed **ISM services survey**
Mar 3 Sa
10:00am

	Nov	Dec	Jan	Feb
Headline composite	56.8	57.6	58.7	<u>58.5</u>
Business activity	59.6	60.5	59.9	
New orders	59.0	58.6	61.8	
Employment	51.5	48.7	55.2	
Prices	63.9	64.4	64.2	

We believe that the ISM services survey's headline composite edged down 0.2pt to 58.5 in February. While the service sector likely will keep recovering over time as the drag from COVID-19 is reduced, the January ISM data looked stronger than some recent figures in other gauges of the service sector, so we expect some moderation in the upcoming report.

Thu **Jobless claims**
Mar 4 Thousands, sa
8:30am

	New claims (wr.)		Continuing claims		Insured Jobless, %
	Wkly	4-wk avg	Wkly	4-wk avg	
Dec 19	806	819	5198	5452	3.5
Dec 26	782	836	5072	5275	3.5
Jan 2	784	816	5175	5192	3.6
Jan 9	927	825	4975	5105	3.5
Jan 16 ¹	875	842	4785	5002	3.4
Jan 23	812	850	4691	4907	3.3
Jan 30	812	857	4558	4752	3.2
Feb 6	848	837	4520	4639	3.2
Feb 13 ¹	841	828	4419	4547	3.1
Feb 20	730	808			
Feb 27	<u>750</u>	<u>792</u>			

1. Payroll survey week

We forecast that initial jobless claims in regular state programs increased 20,000 to 750,000 during the week ending February 27. We think that claims will move lower over time as the drags from COVID-19 ease and the economy recovers. But we also think the data could

be noisy over time, and we expect some of the 111,000 plunge in claims reported for the week ending February 20 to be reversed in the upcoming report.

Thu **Productivity and costs**
Mar 4 Nonfarm business sector, %q/q, saar, unless noted
8:30am

		Rev 3Q20	Prel 4Q20	Rev 4Q20
Productivity	5.1	<u>5.1</u>	-4.8	<u>-4.7</u>
%oya	4.2	<u>4.2</u>	2.5	<u>2.5</u>
Output	44.1	<u>44.1</u>	5.3	<u>5.5</u>
%oya	-3.2	<u>-3.2</u>	-2.7	<u>-2.6</u>
Hourly compensation	-2.2	<u>-4.9</u>	1.7	<u>1.1</u>
%oya	8.2	<u>7.5</u>	7.8	<u>6.9</u>
Unit labor costs	-7.0	<u>-9.5</u>	6.8	<u>6.1</u>
%oya	3.9	<u>3.2</u>	5.2	<u>4.3</u>
Hours	37.1	<u>37.1</u>	10.7	<u>10.7</u>
%oya	-7.1	<u>-7.1</u>	-5.0	<u>-5.0</u>

With a small upward revision already reported for 4Q output, we look for the change in nonfarm productivity in the quarter to be revised up from -4.8% to -4.7% saar. We expect more noticeable revisions to the unit labor costs data based on downward revisions to related compensation figures already released. We believe the 3Q change in unit labor costs will be revised from -7.0% to -9.5% saar and that the 4Q change will be revised from 6.8% to 6.1% saar.

Thu **Factory goods report**
Mar 4 %m/m, sa, unless noted
10:00am

	Oct	Nov	Dec	Jan
New orders	1.3	1.3	1.1	<u>3.4</u>
Shipments	1.2	0.8	1.7	<u>2.6</u>
Inventories	0.3	0.8	0.3	<u>0.3</u>
Inventory/sales ratio	1.41	1.41	1.38	<u>1.35</u>

We estimate that new orders for factory goods increased 3.4% in January while related shipments rose 2.6% and inventories edged up 0.3%. The advance durable goods report already showed solid gains in related orders (3.4%) and shipments (2.0%) in January along with a 0.3% decline in inventories. We expect strong gains in the data for nondurable goods, largely due to increases in prices during the month—we forecast that orders and shipments of nondurable goods jumped 3.3% in January while nondurable inventories increased 1.4%.

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Department of Labor, Federal Reserve Board, ISM, J.P. Morgan forecasts, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

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Economic Research
Global Data Watch

February 26, 2021

J.P.Morgan

Labor market report

Fri	Sa				
Mar 5					
8:30am					
		Nov	Dec	Jan	Feb
Payroll employment					
(ch, m/m, 000s)		264	-227	49	<u>200</u>
Private payrolls		359	-204	6	<u>205</u>
Goods-producing		68	76	-4	<u>40</u>
Construction		24	42	-3	<u>20</u>
Manufacturing		41	31	-10	<u>10</u>
Service-providing		196	-303	53	<u>160</u>
Private service-providing		291	-280	10	<u>165</u>
Wholesale trade		15	16	14	
Retail trade		-2	135	-38	
Professional services		95	156	97	
Temporary help		39	64	81	
Education/health		43	-31	-7	
Leisure and hospitality		10	-536	-61	
Government		-95	-23	43	<u>-5</u>
Average weekly hours		34.8	34.7	35.0	<u>34.8</u>
Index, hrs worked (%m/m)		0.3	-0.5	0.9	<u>-0.4</u>
Hourly earnings (%m/m)		0.3	1.0	0.2	<u>0.3</u>
(%oya)		4.5	5.4	5.4	<u>5.4</u>
Unemployment rate (%)		6.7	6.7	6.3	<u>6.3</u>
Participation rate (%)		61.5	61.5	61.4	

We forecast that nonfarm employment increased 200,000 in February. The level of employment fell on net across December and January with a drop in December followed by a modest pickup in January. But we think that this weakening was in part due to a surge in new COVID-19 cases, and with the US case count coming down noticeably in recent weeks, we think that employment will increase in February.

The jobless claims data don't point to a clear recent change in labor market momentum but these figures haven't been a very reliable guide to the payroll data, and the [December drop in employment](#) looks to be more related to a drop in hiring (that would not necessarily show up in the initial claims data) than an increase in layoffs. Our tracking of some ["alternative" high frequency data measures](#) points to a net gain in February employment of almost 400,000, but with the signal from the more traditional economic indicators less upbeat, we don't expect job growth to be that strong.

For some of the main aggregates within the employment report, we believe that the private sector added 205,000 jobs in February with goods-producing industries adding 40,000 and the service sector adding 165,000. Government payrolls jumped in January, but we think that this was driven by a one-off surge in education-related employment that won't be repeated and we expect a 5,000 decline in government employment in February.

There were some auto plant closures during the reference week for the February employment report but we expect that only several thousand US employees were directly affected so we don't believe that these will have a major impact on the broad national employment readings. More plants reduced their regular work schedules and this could weigh on the hours data. The severe winter weather in Texas and some nearby areas came late in the reference week for the February report and therefore should not impact the BLS's employment count (people are

classified as employed if they receive pay for any part of the pay period associated with the reference week) but we think that the related disruptions could put some downward pressure on hours and upward pressure on average hourly earnings.

Away from the employment count, we think that the average workweek moved down to 34.8 hours in February, reversing much of the jump reported for January. With the workweek expected to decline, we estimate that aggregate hours dropped 0.4% even with the increase anticipated for employment. We also forecast a 0.3% increase for average hourly earnings.

For the household survey, we think there will be increases in employment, the labor force, and the broader population. We believe the unemployment rate held at 6.3% between January and February with the participation rate unchanged at 61.4%. We forecast a tick up in the employment-population ratio from 57.5% to 57.6%.

International trade

Fri				
Mar 5				
8:30am				
		Oct	Nov	Dec
Balance(BOP basis)		-63.8	-69.0	-66.6
Services		18.2	18.0	17.5
Merchandise		-82.0	-87.0	-84.2
Exports (%m/m)		2.2	1.1	3.4
Imports (%m/m)		2.1	2.9	1.5

We believe that the nominal trade balance widened from -\$66.bn in December to -\$67.6bn in January. The advance trade report for January already showed widening in the nominal goods deficit during the month, with increases in exports and imports. We also look for some widening in the real goods deficit, but we think that much of the increase in nominal trade flows was related to price increases in January, and we expect a decline in real goods exports in January along with a modest increase in real goods imports. Services imports have been increasing more rapidly than services exports lately and we believe that continued to be the case into January.

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Department of Labor, Federal Reserve Board, ISM, J.P. Morgan forecasts, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

Review of past week's data

Consumer confidence (Feb 23)

Sa

	Dec	Jan	Feb	
Conference Bd index	87.1	89.3 88.9	89.0 91.3	91.3
Present situation	87.2	84.4 85.5	84.4 92.0	92.0
Jobs plentiful	21.0	20.6 20.0	20.6 21.9	21.9
Jobs hard to get	22.9	23.8 22.5	23.8 21.2	21.2
Labor mkt diff	-1.9	-3.2 -2.5	-3.2 0.7	0.7
Expectations	87.0	92.5 91.2	92.5 90.8	90.8

The Conference Board consumer confidence index increased from 88.9 in January to 91.3 in February. This measure has picked up modestly in recent months but remains down substantially from the figures reported before the pandemic began, and the latest data are on the low end of the range reported since the pandemic-related plunge in sentiment. Within the Conference Board survey, the labor market differential improved from -2.5 in January to +0.7 in February. This gauge of the job market has improved noticeably off of the recent low of -15.7 reported for last April, but it still looks depressed relative to the figures reported before the pandemic began. And even with the recent increase, the February figure was still weaker than what was reported between September and November last year.

New home sales (Feb 24)

	Nov	Dec	Jan	
Total (000s, saar)	829 839	842 885	860 923	923
%m/m	-12.6 -13.1	-1.6 5.5	-2.4 4.3	4.3
%oya nsa	18.0	-12.2 20.4	-11.1 18.6	18.6
Months' supply	-4.2 4.1	-4.3 4.1	-4.4 4.0	4.0
Median price (%oya)	-4.8 6.6	-8.0 7.2	-8.0 5.3	5.3

New single-family home sales increased 4.3% to 923,000 saar in January. This report was stronger than anticipated both in terms of the January data and upward revisions to earlier figures. While sales have cooled somewhat relative to their recent high (979,000 saar last July) the recent sales rates have remained strong through some ups and downs in the monthly figures. And many other housing indicators also show strong levels of activity lately even if there has been some recent moderation.

Durable goods (Feb 25)

%m/m, sa

	Nov	Dec	Jan	
New orders	1.3	-0.5 1.2	-1.1 3.4	3.4
Ex transportation	1.0	-1.1 1.7	-1.0 1.4	1.4
Nondef cap. gds ex air	1.2	-0.7 1.5	-0.6 0.5	0.5
Shipments	0.4	-1.7 2.1	-1.5 2.0	2.0
Nondef cap. gds ex air	0.4	-0.7 1.0	-0.6 2.1	2.1
Inventories	0.9	-0.2 -0.3	-0.2 -0.3	-0.3

Several details of the January durable goods report came out well above expectations, including the headline orders figure (+3.4%) and the increase in core capital goods shipments (2.1%) for the month. The January increase in core capital goods orders was more modest and closer to expectations, but still solid (at 0.5%). Overall, the key series related to equipment investment appear to have solid momentum early this year, and while there is still plenty we don't know about activity in 1Q as a whole, we think that real growth in equip-

ment spending will be strong in 1Q, perhaps even above the 19% saar figure we have penciled into our GDP forecast.

Gross domestic product (Feb 25)

%ch, q/q, saar, unless noted

	3Q20	Adv 4Q20	Sec 4Q20	
Real GDP	33.4	4.0	4.5 4.1	4.1
Final Sales	25.9	3.0	3.1 3.0	3.0
Domestic final sales	29.8	4.4	4.8 4.4	4.4
Consumption	41.0	2.5	2.6 2.4	2.4
Equipment	68.2	24.9	25.9 25.7	25.7
Intellectual property	8.4	7.5	7.4 8.4	8.4
Nonres. structures	-17.4	3.0	1.8 1.1	1.1
Residential investment	63.0	33.5	36.8 35.8	35.8
Government	-4.8	-1.2	0.9 -1.1	-1.1
Exports	59.6	22.0	21.5 21.8	21.8
Imports	93.1	29.5	29.3 29.6	29.6
Inventories (ch, \$bn)	-3.7	44.6	59.3 48.0	48.0
Net exports-pct.pt.contr.	-3.2	-1.5	-1.7 -1.6	-1.6
Inventories-pct.pt.contr.	6.6	1.0	1.4 1.1	1.1
Core PCE price index	3.4	1.4	1.4 1.4	1.4
(%oya)	1.4	1.4	1.4 1.4	1.4
GDP chain price index	3.5	2.0	2.1 2.1	2.1
(%oya)	1.1	1.3	1.3 1.3	1.3
Adj. corporate profits	27.4			
(%oya)	3.5			

The BEA revised its estimate of 4Q real GDP growth up from 4.0% to 4.1% saar. The revisions to the main growth components also were pretty modest and real final sales growth was unchanged after rounding at 3.0% saar. The upward revision to the headline growth figure was largely due to an upward revision to the 4Q change in inventories. Overall, these revisions didn't meaningfully change our thinking on 4Q growth or how things stood headed into 1Q.

Revisions also were pretty modest on the price front, with annualized quarterly growth in the GDP deflator and headline PCE price index revised up by a tenth and no revision to the change in the core PCE price index after rounding (at 1.4% saar). The drops in income reported for 3Q and 4Q both were revised lower, with the updated 4Q saving rate now at 13.0% (vs. 13.4% before today's revisions).

Pending home sales (Feb 25)

sa, unless noted

	Nov	Dec	Jan	
Total (mn, ar)	125.9 125.8	125.5 126.4	122.4 122.8	122.8
%ch m/m	-2.5 -0.9	-0.3 0.5	-2.5 -2.8	-2.8
%oya (nsa)	16.1	-22.8 23.1	-12.4 8.2	8.2

The pending home sales index fell 2.8% in January, disappointing the consensus forecast but coming out pretty close to our expectations. Through some ups and downs in the data in recent months, the index has fallen somewhat since the recent peak level from August. But the level of activity has remained strong even with this recent cooling. Pending home sales tend to lead existing home sales by one or two months, so the existing home sales data likely will moderate soon (while remaining at a solid level).

Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Department of Labor, Federal Reserve Board, ISM, J.P. Morgan forecasts, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

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February 26, 2021

J.P.Morgan**Personal income (Feb 26)**

%m/m, sa, unless noted

	Nov	Dec	Jan	
Personal income	-1.3	-1.2	0.6	10.3 10.0
Wages & salaries	-0.4	0.5	0.5	0.7 0.7
Consumption	-0.7	-0.6	-0.2 -0.4	-2.3 2.4
Real consumption	-0.7	-0.6	-0.6 -0.8	-1.8 2.0
PCE price index	0.0	0.4	-0.5	0.3
Core	0.00	0.34	0.30	0.38 0.25
Mkt-Based Core	0.0	0.2		0.3
Core (%oya)	1.4	-1.5	1.4	-1.7 1.5
Mkt-Based Core	1.3	1.3		1.4
Saving rate	12.9	12.5	13.7	13.4 20.8 20.5

Real consumer spending jumped 2.0% in January, a strong increase that was close to expectations. The retail sales report already had signaled that spending picked up in January following the slump late in 2020 and this more complete measure of consumer activity now reported by the BEA similarly shows a jump in spending early this year after declines late last year. We think the trajectory for spending through January makes it likely that real consumption growth will be strong in 1Q although realized outlays will depend in part on what happens with the potential upcoming stimulus package.

The January increase in consumer spending was almost certainly tied to the surge in income coming from federal support during the month. Nominal income jumped 10.0% in January, but actually edged down slightly excluding transfer receipts. Among the transfer receipts, stimulus checks accounted for about \$1.7tr of income in January and the supplement to UI payments authorized as part of the December stimulus package accounted for about \$300bn (both of these figures reported in annualized terms). Even though spending jumped in January, the saving rate increased from 13.4% in December to 20.5% on this massive influx of income.

In terms of prices, the core PCE price index increased 0.3% in January. This was a decent amount above consensus expectations but somewhat below our forecast. Even with this solid monthly gain, the broader core PCE price trend remained modest at 1.5% oya. The headline PCE price index also rose 0.3% in January and was up 1.5% oya.

Consumer sentiment (Feb 26)

	Jan	Pre Feb	Fin Feb	
Univ. of Mich. Index	79.0	76.2	76.0	76.8
Current conditions	86.7	86.2		86.2
Expectations	74.0	69.8		70.7
Inflation expectations				
Short term	3.0	3.3		3.3
Long term	2.7	2.7		2.7

International trade (adv.) (Feb 26)

\$bn, samr, unless noted

	Nov	Dec	Jan	
Balance of goods, Cen.	-86.1	-83.2	-82.7	-83.7
Exports (%samr)	1.1	4.6	4.5	1.4
Imports (%samr)	3.1	1.4	0.7	1.1

The nominal trade balance widened from -\$83.2bn in December to -\$83.7bn in January, with net exports looking like they are on track to be a drag on growth in 1Q (very early in the quarter).

Business inventories (adv.) (Feb 26)

%m/m, sa, unless noted

	Nov	Dec	Jan	
Wholesale	0.0	-0.3	0.5	-0.4 1.3
Retail inventories	0.7	-1.2	1.9	-0.0 -0.6
Ex autos	0.3	-1.2	2.2	-0.4 -0.2
Autos	1.8	1.1	-0.9	-1.4

The inventory data have been a mixed bag lately, and the advance economic indicators report showed a 1.3% jump in wholesale inventories and a 0.6% drop in retail inventories.

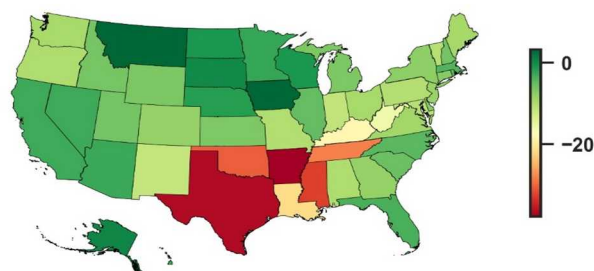
Sources: ADP/Moody's Analytics, BEA, BLS, Census Bureau, Conference Board, Department of Labor, Federal Reserve Board, ISM, J.P. Morgan forecasts, NAHB, NAR, NFIB, NY Fed, Markit, Philadelphia Fed, Standard & Poor's, University of Michigan, US Treasury

Focus: Heat maps feel the Texas chill

Cold temperatures and related disruptions have led to a sharp pullback in some high-frequency economic data in Texas and neighboring states (Figure 1). This localized shock has been large enough to impact some national high-frequency data, but effects on traditional monthly and quarterly economic indicators will depend on how long the disruptions last and how fast activity bounces back. We think the disruptions will prove temporary and the broader economic recovery remains on track.

Figure 1: Chase consumer card spending

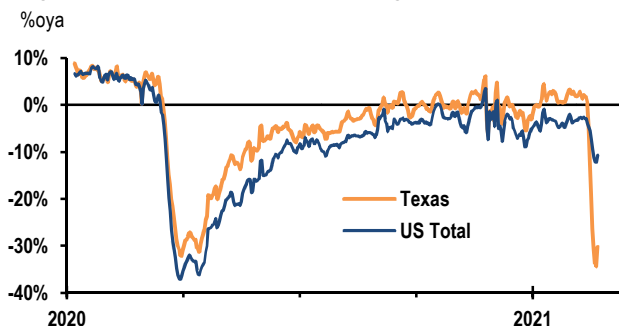
Change in % oya growth since February 10



Source: J.P. Morgan

Our [Chase consumer card spending tracker](#) for Texas has fallen sharply since the severe winter weather in the region started. The seven-day average of total spending was down about 35% oya in the data through February 20, a larger percentage decline than the nadir early in the pandemic (Figure 2). With spending also down sharply in some neighboring states, our national aggregate of card spending has fallen significantly.

Figure 2: Chase consumer card spending tracker



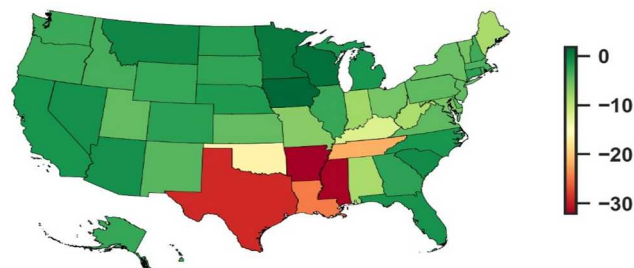
Source: J.P. Morgan. Texas data exclude airline spending.

Localized shocks like this are also visible in a variety of other high-frequency data, including OpenTable diners, Apple driving direction requests, and Google's measure of workplace mobility (Figure 3). Our state-level job trackers based on alternative data combine a collection of these indicators into

one signal about economic activity in each state. These trackers similarly show sharp declines in several states that were hit by severe weather, but recent changes have been much more favorable in other parts of the country. We therefore think that the broader economic recovery remains on track and that any weakness we may see in upcoming economic reports is likely driven by temporary weather-related issues.

Figure 3: Google workplace mobility

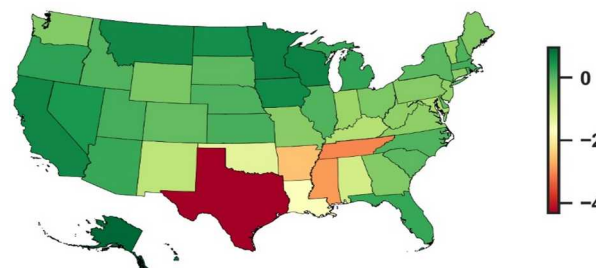
Change since February 10



Source: Google, J.P. Morgan

Figure 4: Job tracker based on alternative data

% change since February 10



Source: Various sources, J.P. Morgan

Interestingly, initial claims for unemployment insurance did not rise sharply in the most-affected states in the latest data for the week ending February 20. It is possible that the weather interfered with claims filings and that we will still see a spike in claims in the coming weeks. But it is also possible that the weather disruptions will prove too fleeting to meaningfully impact the labor market, and indeed there are already signs of the rebound beginning. The state-level job trackers are updated daily in the [US Quant Econ Dashboard](#).

We should also keep in mind that the BLS's February employment report uses the week ending February 13 as a reference week. With the bad weather not coming until late in that week, we think that the figures related to employment (which count anyone who received pay for any part of the related pay period as employed) should not be impacted by the weather, although some other details from the report might be.

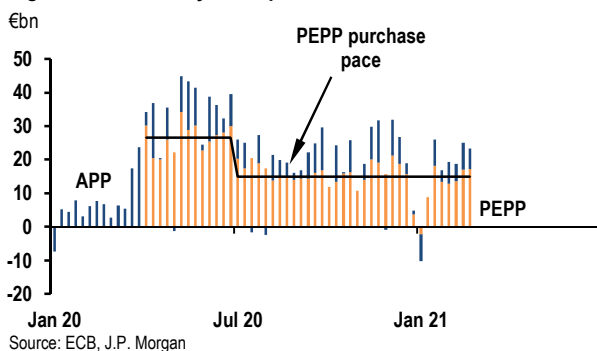
Euro area

- **ECB monitoring long-term bond yields**
- **EC sentiment rose in February, but remains significantly below its pre-virus level**
- **German 4Q GDP revised up**
- **National releases hint at February core inflation decline**

ECB president Lagarde spoke at a plenary session in the European Parliament on Monday and used the opportunity to comment on the recent rise in sovereign yields. She said that the ECB is looking at a broad set of indicators to assess whether financing conditions are still favorable and that risk-free OIS rates and sovereign yields play a particularly important role in this. She then added that “the ECB is closely monitoring the evolution of longer-term nominal bond yields.”

As she was making these comments, the ECB published data on the APP and PEPP for last week (Figure 1). The outstanding amount of PEPP purchases increased by €17bn, assuming there were no distortions from lumpy redemptions. Hence, after three weeks of €13bn increases, the ECB may have stepped up the pace of PEPP purchases somewhat. However, the significance of this move is not entirely clear-cut. First, the ECB purchased at a €27bn/week pace in 2Q20 and is therefore still much closer to the €15bn/week average since last July. Second, the ECB needs to maintain a €17bn/week pace if it is to fully use up the PEPP envelope by March 2022. Hence, the recent increase only puts the ECB back on that pace. And, that pace still leaves the ECB’s staff’s inflation forecasts far below the target.

Figure 1: ECB weekly asset purchases



Hence, at this stage, the signal regarding the ECB’s response is still unclear. In recent months, the ECB has “closely monitored” movements in the currency, but without following through with a deposit rate cut. The lack of action likely reflected that the political economy around negative interest

rates has become difficult. By contrast, it is easier for the ECB to respond to a rise in bond yields as it can simply use the flexibility of PEPP. However, the definition of “financing conditions” is very broad and not all ECB policymakers will necessarily regard the latest increases as “unwarranted.” Hence, it is not yet clear whether and how forcefully the ECB is responding beyond this week’s verbal intervention. At the latest, the March meeting in two weeks’ time should provide clarity on this. Alternatively, a step up in the weekly flow of purchases back to (or close to) the 2Q20 pace would send a clear signal that the ECB is not minded to allow a significant backup in nominal yields at this stage, even if it is accompanied by gains in risky asset prices.

ESI survey broadly aligned with PMI

The EC economic sentiment indicator rose 1.9pts to 93.4 in February, which leaves it about 10pts below the average of the January and February readings last year. The EC survey and its details are broadly aligned with the PMI survey (Figure 2): in the EC survey there is a significant gap between the manufacturing index (up 2.8%-pts to -3.3%bal) and services index (up 0.6%-pt to -17.1%bal), and shows that Germany is doing best among the main economies of the region. Regarding the retail sector (not available in the PMI survey), the headline index declined 0.6%-pt to 19.1%bal. Both the services and retail sectors have been hit hard by virus-related restrictions while restrictions had little impact on the manufacturing side in recent months (Figure 3). An interesting observation is the 4.4pts rise in the Italian composite survey to 94.6 as Draghi took office, which hints at a rise in the Italian PMI (the ex. Germany and France flash PMI index was up 2pts to 47.2 last week). Overall, business surveys have not been very useful indicators of activity since the virus outbreak. We note however that the broad stability of these indicators since the start of the year echoes the broad stability of restrictions in the region.

Figure 2: Euro area EC economic sentiment and PMI

Standard deviations from 2000-2007 mean

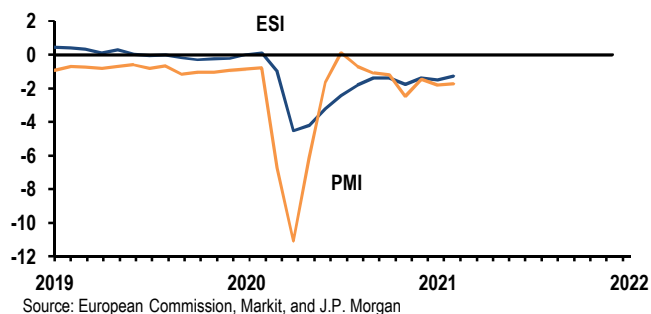
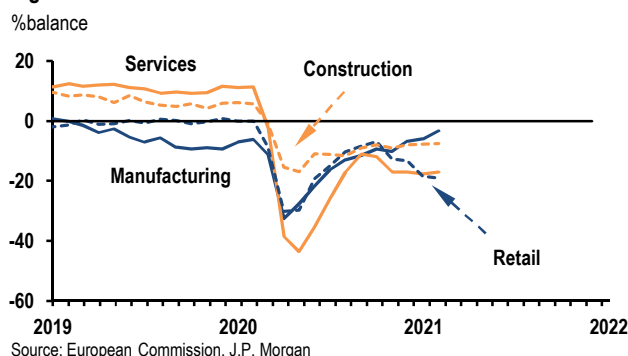


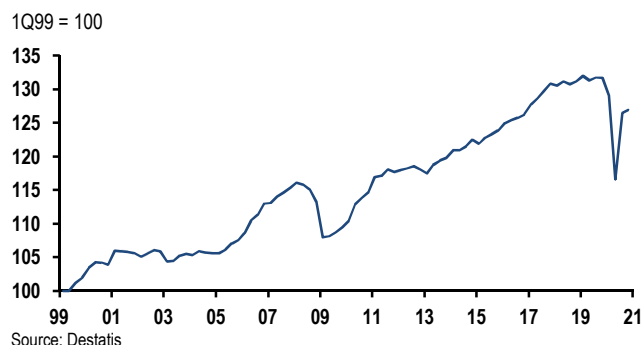
Figure 3: Euro area EC sentiment indicator



German GDP grew 1.4% ar in 4Q20

German 4Q20 GDP was revised up by 0.25% in this week's final report, with growth now reported at 1.4%/q, saar (vs. 0.4%/q, saar in the flash report). This leaves 4Q GDP 3.6% below the 4Q19 level (Figure 4). Moreover, despite the increase in 4Q20, GDP on a weekly basis was lower at the end of the quarter than at the start. This creates a trajectory into 1Q21 that makes a likely. We still project a 5%/q, saar contraction, but the upward revision to 4Q20 GDP creates some upside risk to this.

Figure 4: German real GDP



The new details show that the GDP decline mostly was due to a 12.7%/q, saar nose-dive in consumer spending and, to a lesser extent, to a 2% decline in government consumption. By contrast, capex rose 4.2%/q, saar in 4Q20 and trade flows also firmed further. Overall, this resulted a big 6.5%-pts drag from domestic final sales, offset by a large 5.8%-pts contribution from inventory changes and 2.4%-pts from net trade. We note, however, that inventory accumulation is still running at a slow pace, with the 4Q20 bounce only undoing a big drag in 3Q20. On the production side, value added jumped by 28%/q, saar in the industrial sector and by 23%/q, saar in construction. Private services output declined by almost 10%/q, saar, reflecting a more concentrated hit in those sectors directly affected by the new restrictions. For example, business services value added declined only 2.2%/q, saar in 4Q20, whereas it had slumped almost 40%/q, saar in 2Q20.

A few more aspects of the report are worth noting. The household saving rate had surged from around 11.5% before the crisis to a 20.3% peak in 2Q20, fell to 15% in 3Q20 and then jumped back to almost 18% in 4Q20. A large part of this growth in savings likely reflects forced savings, even though the VAT cut should have supported some categories of consumer spending in 4Q20. In the labor market, employment edged up in 4Q20 while hours worked slumped 7.7%/q, saar, reflecting renewed use of workweek flexibility (including the short-time work subsidies). Interestingly, compensation per employee nevertheless rose 2.5%/q, saar in 4Q20, despite the cut in hours worked, contributing to another increase in household disposable income in 4Q20.

Core inflation likely to decline in February

The details released on Tuesday were important to assess the drivers of the January core inflation jump. In particular, we have [pointed out](#) the important role of the German VAT rebound, the impact of new weights in the basket, and delayed winter sales. These factors will play a role in shaping Euro area core inflation this year. Regarding the German VAT rebound, the drag seen in 2H20 (worth close to 0.5%-pt) has now disappeared, but a temporary base effect will lift Euro area core inflation by about 0.5%-pt in 2H21. Meanwhile, we [laid out a scenario](#) where the upward distortion coming from weight changes in January (worth 0.4%-pt) would fade in the coming months and potentially turn negative this summer, before turning positive again toward the end of the year. But this impact is very hard to assess. Finally, we think the upward distortion from the winter sales (worth 0.4%-pt) will start to fade in February and will have disappeared by March.

The February preliminary data for France and Spain released on Friday are interesting to assess in light of these drivers. The information so far is limited but the CPI details (according to our calculation) point to a 0.5%-pt decline in French core inflation to 0.3%oya and a 0.3%-pt decline in Spanish core inflation to 0.3%oya. In France, we think that the sales distortion largely unwound in February. In Spain, the data did not show a large increase in clothing price inflation in January and our calculation implied that the distortion coming from weight changes was small. According to the statistics office, the core inflation decline in February is linked to holiday-related items (including accommodation services and package holidays). Together, France and Spain represent 32% of the HICP basket. The German data on Monday (28% of the basket) will be very important to assess as distortions in January were particularly acute.

The limited details for France and Spain are only available at the CPI level and are hard to translate into HICP. But the information so far is broadly aligned with our view that Euro area core inflation is set to decline by 0.4%-pt to 1.0%oya.

Data releases and forecasts

Week of March 1 - 5

Output and surveys

Purchasing managers index final (manufacturing)

		Nov	Dec	Jan	Feb
Mon	Euro area				
Mar 1	Overall region	53.8	55.2	54.8	<u>57.7</u>
10:00am					
9:55am	Germany	57.8	58.3	57.1	<u>60.6</u>
9:50am	France	49.6	51.1	51.6	<u>55.0</u>
9:45am	Italy	51.5	52.8	55.1	
9:15am	Spain	49.8	51.0	49.3	

Purchasing managers index final (services)

		Nov	Dec	Jan	Feb
Wed	Euro area				
Mar 3	Overall region	41.7	46.4	45.4	<u>44.7</u>
10:00am					
9:55am	Germany	46.0	47.0	46.7	<u>45.9</u>
9:50am	France	38.8	49.1	47.3	<u>43.6</u>
9:45am	Italy	39.4	39.7	44.7	
9:15am	Spain	39.5	48.0	41.7	

Purchasing managers index final (composite)

		Nov	Dec	Jan	Feb
Wed	Euro area				
Mar 3	Overall region	45.3	49.1	47.8	<u>48.1</u>
10:00am					
9:55am	Germany	51.7	52.0	50.8	<u>51.3</u>
9:50am	France	40.6	49.5	47.7	<u>45.2</u>
9:45am	Italy	42.7	43.0	47.2	
9:15am	Spain	41.7	48.7	43.2	

According to the flash release, the Euro area composite PMI was up marginally in February and we expect this number to be confirmed next week. After a near 5pt fall in November to 45.3, the PMI rebounded by around 4pts to 49.1 in December, and settled close to the 48 mark at the start of the year. This pattern echoes changes in restrictions in the region. Although restrictions are determined at the national level and show huge differences (qualitatively and in terms of timing), these restrictions were overall tightened substantially in November (in France in particular and to some extent Italy), and were eased at the start of December. Germany then tightened restrictions significantly in late December, and restrictions have since been broadly unchanged in countries covered by the PMI survey.

Manufacturing orders

		Oct	Nov	Dec	Jan
Fri	Germany				
Mar 5	Volumes, sa				
8:00am	Total (%m/m)	3.4	2.7	-1.9	<u>0.0</u>
	%oya	2.6	6.8	6.4	
	Total ex. bulk orders (%m/m)	1.8	2.2	-2.0	<u>0.0</u>
	%oya	4.8	6.8	5.7	
	Domestic (%m/m)	3.3	2.4	-0.9	
	%oya	4.8	6.2	4.3	

Foreign (%m/m)	3.4	2.9	-2.6
%oya	0.9	7.2	7.9

German orders rose strongly in 4Q20 (31.1%q/q, saar) and the December level was 2% above the pre-COVID-19 level. The German manufacturing PMI suggests that new orders remained strong at the start of the year. In fact, after a near-4pt fall in January, the new orders index fully reversed this decline in February and increased back to a very high 62.1pts. It is possible that actual orders will fall in January if some orders were pulled forward ahead of Brexit and if carmakers had slowed some orders of parts due to the semiconductor shortages. The expiry of the lower VAT rate may also have created a drag on car orders. However, overall we think that orders were likely stable in January.

Real GDP

		1Q20	2Q20	3Q20	4Q20
Wed	Italy (final)				
Mar 3	%q/q, sa	-5.5	-13.0	16.0	<u>-2.0</u>
10:00am	%q/q, saar	-20.4	-42.8	80.9	<u>-7.7</u>
	%oya	-5.6	-18.1	-5.1	<u>-6.6</u>
	GDP components (%q/q, saar)				
	Private consumption	-24.6	-38.6	59.7	
	Government consumption	-4.5	1.4	3.0	
	Fixed investment	-27.0	-52.4	196.8	
	Exports	-28.0	-66.5	191.5	
	Imports	-19.5	-54.2	80.2	
	Contribution to GDP growth (%q/q, saar)				
	Domestic final sales	-21.1	-34.0	63.7	
	Inventories	4.8	-3.8	-4.1	
	Net trade	-3.8	-8.6	16.5	

Demand and labor markets

Unemployment

		Oct	Nov	Dec	Jan
Thu	Euro area				
Mar 4	Harmonized measure (Eurostat)				
11:00am	Unemployment rate (% sa)	8.4	8.3	8.3	<u>8.3</u>
	Unemployment (ch m/m, 000s)	-197.0	-233.0	55.0	

Part-time work subsidy schemes have to a large extent shielded labor markets from the negative consequences of the virus outbreak. During last year, the Euro area unemployment rate was only up 1%-pt to 8.3% while GDP was down 6.8%. Part-time work subsidy schemes are still in place at the start of this year, thus the impact of restrictions (in the hospitality sector and sometimes non-essential retail shops) will be dampened. Overall, we expect the Euro area unemployment rate to remain stable, as was the case in recent months.

		Nov	Dec	Jan	Feb
Tue	Germany				
Mar 2	Registered (ch m/m, 000s, sa)	-42	-40	-41	<u>0</u>
9:55am	000s, nsa	2699.1	2707.2	2900.7	
	Unempl. rate (% sa)	6.1	6.0	6.0	<u>6.0</u>

Source: European Commission, Eurostat, ECB, FSO, Bundesbank, IFO, INSEE, ISAE, Istat, INE, CBS, BNB, Markit, and J.P. Morgan forecasts

Employment

		Oct	Nov	Dec	Jan
Tue	Germany				
Mar 2	Change m/m, 000s, sa	18	-26	10	<u>0</u>
9:55am					

The German labor market was surprisingly firm in January, with a large fall in unemployment and a rise in employment. Short-time work applications did increase due to the additional closures in the retail sector. But, overall we expect the recent resilience to have continued in the February report with stable outturns.

Retail sales

		Oct	Nov	Dec	Jan
Thu	Euro area				
Mar 4	Total sales, volumes				
11:00am	%m/m, sa	1.4	-5.7	2.0	<u>-2.3</u>
	%oya, working-day adj.	4.3	-2.2	0.6	

After a 5.7%/m/m fall in November (largely due to restrictions in France, Italy, and Belgium), Euro area retail sales rebounded in December. The Euro area rebound was modest, however (2.0%/m/m) as Germany shut non-essential retail stores around mid-month leading to a 9.1%/m/m retail sales decline in this country. In January, we expect retail sales to fall 2.3%/m/m. This fall is largely concentrated in Germany (due to restrictions) and France (some payback after the December jump).

		Oct	Nov	Dec	Jan
Tue	Germany				
Mar 2	Sales ex. autos and petroleum, volumes, sa				
8:00am	%m/m	2.9	1.6	-9.1	<u>-2.0</u>
	%oya	8.5	9.0	0.2	

German retail sales fell sharply in December. While the temporary VAT cut should still have provided support, the closure of all nonessential retail stores in mid-December was likely a big drag. Nevertheless, it is remarkable that retail sales were still up in 4Q20 overall. Retail shops remained closed in January and therefore retail sales may have fallen a bit further last month. But, in an underlying sense, household savings have increased sharply in recent quarters and this should provide support once shops reopen.

Inflation**Consumer prices**

		Nov	Dec	Jan	Feb
Tue	Euro area (flash)				
Mar 2	HICP (%oya, nsa)	-0.3	-0.3	0.9	<u>0.8</u>
11:00am	HICP core (%oya, nsa)	0.2	0.2	1.4	<u>1.0</u>

See Euro area essay for details.

		Nov	Dec	Jan	Feb
Mon	Germany (prelim)				
Mar 1	%m/m, nsa	-0.8	0.5	0.8	<u>0.5</u>
2:00pm	%oya	-0.3	-0.3	1.0	<u>1.2</u>
	HICP (%oya)	-0.7	-0.7	1.6	<u>1.8</u>
	Baden Wuerttemberg (%oya)	0.1	0.1	1.1	<u>1.3</u>
	Bavaria (%oya)	-0.2	-0.3	1.4	<u>1.3</u>
	Brandenburg (%oya)	-0.2	-0.1	1.3	<u>1.4</u>
	Hesse (%oya)	-0.6	-0.5	0.9	<u>0.8</u>
	North-Rhine West (%oya)	-0.4	-0.4	1.0	<u>1.1</u>

		Nov	Dec	Jan	Feb
	Saxony (%oya)	0.1	0.0	1.0	<u>1.1</u>

Mon	Italy (prelim)				
Mar 1	%m/m, nsa	-0.1	0.2	0.7	<u>0.3</u>
11:00am	%oya, nsa	-0.2	-0.2	0.4	<u>0.8</u>
	HICP (%oya, nsa)	-0.3	-0.3	0.7	<u>0.6</u>

Producer prices

		Oct	Nov	Dec	Jan
Wed	Euro area				
Mar 3	%m/m, nsa	0.4	0.4	0.8	
11:00am	%oya, nsa	-2.0	-1.9	-1.1	-

Review of past week's data**Output and surveys****European Commission survey**

	Dec	Jan	Feb
Euro area			
% balance of responses, sa			
Economic confidence	92.4	91.5	<u>94.5</u> 93.4
Industrial confidence	-6.8	-5.9 -6.1	-3.3
Construction confidence	-8.0	-7.7	-7.5
Retail confidence	-12.9 -13.2	-18.9 -18.5	-19.1
Service confidence	-17.1	-17.8 -17.7	-17.1
Consumer confidence	-13.8	-15.5	-14.8

See Euro area essay for details.

National business surveys

	Dec	Jan	Feb
German IFO survey			
2015=100, sa			
Business climate	92.2	<u>90.4</u> 90.3	<u>94.0</u> 92.4
Business situation	91.3	89.2	<u>89.5</u> 90.6
Business expectations	93.0	<u>94.4</u> 91.5	<u>92.5</u> 94.2

The German IFO improved solidly in February (+2.1 to 92.4), reversing the January fall and putting the IFO back very close to the October level (i.e., the pre-lockdown level). Encouragingly, the improvement was driven by the expectations index, which rose almost 3pts to 94.2, while the current conditions index improved by less (+1.4pts to 90.6). By sector, the improvement was broad-based, led by a large gain in manufacturing. In terms of the implications, it remains difficult to link the surveys to changes in the level of GDP and the current level is still low historically. However, it can be seen as encouraging that the IFO improved in February even though the lockdown was not eased in the month and even though German industry is facing some disruptions from shortages of semiconductors, from higher transport costs, and from border controls.

	Dec	Jan	Feb
France (INSEE survey - manufacturing)			
Index			
Composite index	94.3	<u>98.2</u> 96.0	97.4
Index of past production	4.8	<u>42.4</u> 6.2	5.0
Exp. output - personal	4.8	<u>7.2</u> 7.8	10.2
Exp. output - general	-4.8	<u>-9.2</u> -9.6	-7.6

Source: European Commission, Eurostat, ECB, FSO, Bundesbank, IFO, INSEE, ISAE, Istat, INE, CBS, BNB, Markit, and J.P. Morgan forecasts

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Economic Research**Global Data Watch**

February 26, 2021

J.P.Morgan

	Dec	Jan	Feb	
Italy (ISAE survey)				
2000=100, sa				
Producer confidence	96.0	96.4	95.4	95.6 99.0

Real GDP**Germany**

	2Q20	3Q20	4Q20	
%q/q, sa	-9.7	8.5	0.1	0.3
%q/q, saar	-33.5	38.6	0.4	1.4
%oya	-11.2	-4.0	-3.0	-3.6

GDP components (%q/q saar)

Private consumption	-37.6	-37.2	50.8	50.5 -12.7
Government consumption	9.4	8.5	3.4	2.3 -2.0
Mach, equip, other investment	-48.0	-48.1	81.3	80.2 -0.5
Construction investment	-16.0	-16.1	-7.6	-5.0 7.5
Exports	-60.0	-59.9	94.8	93.8 19.5
Imports	-50.0	-49.9	41.5	41.2 15.7

Contribution to GDP growth (%q/q saar)

Domestic final sales	-24.7	-24.6	29.3	-6.5
Inventories	0.5	0.4	-8.4	-8.2 5.8
Net trade	-11.4	47.2	17.0	2.4

See Euro area essay for details.

	2Q20	3Q20	4Q20	
France (3rd estimate)				
%q/q, sa	-13.7	-13.5	18.5	-1.3 -1.4
%q/q, saar	-44.4	-44.0	97.2	96.9 -5.3 -5.7
%oya	-18.8	-18.6	-3.9	-3.7 -5.0 -4.9
GDP components (%q/q saar)				
Private consumption	-40.4	-39.9	99.2	98.7 -20.0 -20.7
Government consumption	-34.3	-34.2	72.8	72.4 -1.4 -1.2
Fixed investment	-47.0	-47.9	136.3	136.9 10.0 4.6
Exports	-68.7	-68.4	120.9	122.5 20.6 25.3
Imports	-52.6	-52.8	82.4	83.5 5.1 7.5
Contribution to GDP growth (%q/q saar)				
Domestic final sales	-40.9	-41.0	104.3	103.7 -10.3 -11.2
Inventories	3.4	3.8	-6.8	1.6 1.7
Net trade	-8.4	-8.1	2.9	3.0 4.3

France (prelim)

%m/m, nsa	0.2	0.2	-0.3	-0.1
%oya, nsa	0.0	0.6	0.3	0.4
HICP (%oya)	0.0	0.8	0.5	0.7

Spain (flash)

%m/m, nsa	0.2	0.0	0.3	-0.6
%oya, nsa	-0.5	0.5	0.8	0.0
HICP (%oya, nsa)	-0.6	0.6	0.7	-0.1

Source: European Commission, Eurostat, ECB, FSO, Bundesbank, IFO, INSEE, ISAE, Istat, INE, CBS, BNB, Markit, and J.P. Morgan forecasts

Demand and labor markets**Domestic consumption**

	Nov	Dec	Jan	
France				
Consumption of goods, volumes, swda				
%m/m	-18.0	-17.9	23.0	22.4 -4.6
%oya	-46.0	-15.6	3.7	3.6 0.0

Inflation**Consumer prices**

	Nov	Dec	Jan	
Euro area (final)				
HICP (%m/m, nsa)	-0.3	0.3	0.2	
HICP (%oya, nsa)	-0.3	-0.3	0.9	
HICP (%oya, core-XX) ¹	0.2	0.2	1.4	
HICP (%m/m, ex-tob.)	-0.4	0.3	0.2	

See Euro area essay for details.

Japan

- We now expect the contraction in 1Q21 to be modest, with solid exports and production activity
- Jan IP surprised to upside, rising 4.2%*m/m*, *sa*, pointing to a broader production recovery
- We expect consumption to be a less of a drag on 1Q growth, and capex recovery to continue
- Nationwide core CPI likely will slip into deflation in 1H21, before returning to 0.0% by year-end

We continue to look for a GDP contraction in 1Q21, but now expect a smaller drag compared to our previous projection. With strong global demand, exports were firm at the start of the year, leading a sustained recovery in manufacturers' business sentiment. This week's January industrial production and retail sales data also point to a strong production recovery and resilient goods consumption, despite the renewed state of emergency. We now expect consumption to be less of a drag, in 1Q strong production to lead a further recovery in capex, which remained depressed compared to the pre-pandemic level even after a 14.9%*q/q*, *saar* jump in 4Q. Thus, the modest contraction we expect in 1Q GDP mainly is attributable to private consumption, especially for services, which likely will remain weak with the extended state of emergency and subsequent self-isolation until people regain confidence that the virus is coming under control.

This week brought some positive developments in COVID-19 restrictions. As the number of infections has fallen sharply since late January (Figure 1), the government decided to lift the state of emergency for all prefectures except those in the Metropolitan Tokyo area at the end of February, a week earlier than initially scheduled. Although business restrictions likely still will be removed only gradually, this should provide a strong base for the expected consumption recovery from 2Q. We expect the virus to become less of a drag on the economy over time, while the expected bounce in global demand, especially from the US, should support Japan's exports. We expect economic activity to return to the level of 4Q19, the quarter after the consumption tax hike and before the pandemic, by mid-2021, followed by a further recovery to the 2Q19 level, which we think is the better pre-pandemic benchmark for Japan, by year-end.

We also revised up our nationwide core CPI forecast by 0.1%-0.2%-pt in 2021 and 2022. We expect nationwide core CPI inflation to fall into negative territory at -0.1%*o/a* in 1Q and decline further to -0.8%*o/a* in 2Q, before returning to 0.0% in 4Q20 (Figure 2). Although we look for underlying inflation to bottom in 2Q reflecting the expected economic recovery, some policy factors, such as the resumption of the

government travel subsidy program and an expected cuts in mobile phone charges, likely will drag on core inflation further this year. In addition to the upward revision of the BoJ core CPI, we also raised our core CPI (ex. fresh food) forecast by 0.3%-pt to 0.4%*o/a* in 4Q20, reflecting the rises in the current and future oil prices.

Figure 1: COVID-19 new cases and mobility

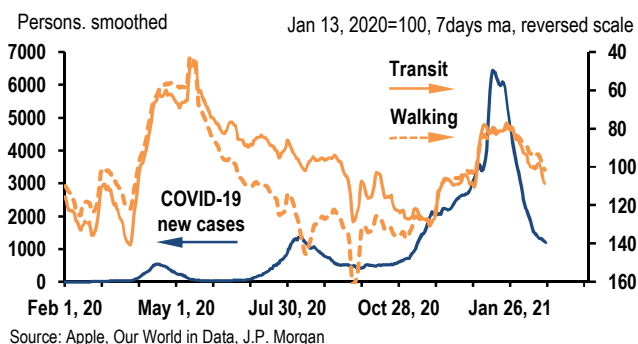
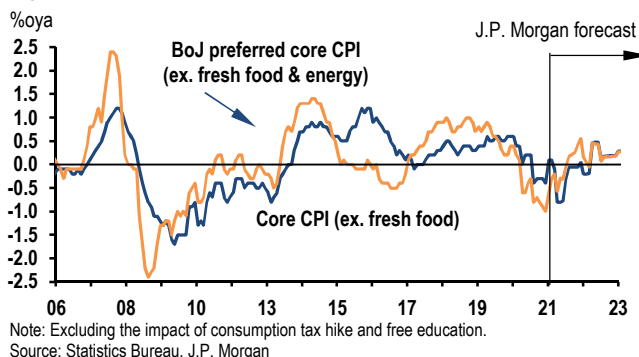


Figure 2: Core CPI forecast



A strong IP gain in January

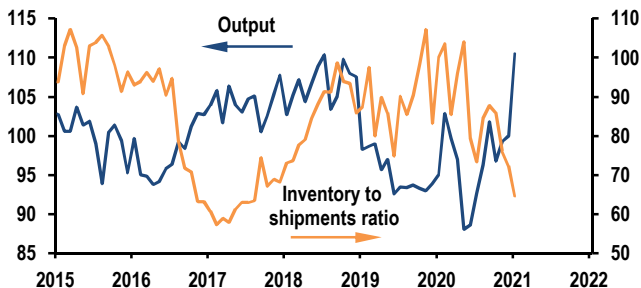
January industrial production surprised to upside, jumping 4.2%*m/m*, *sa*. We expected a modest 0.5% decline, despite the strong manufacturers' projections reported earlier, as in mid-January some automakers announced a cut in production for a few months due to the global supply shortage of semi-conductors. However, auto production remained resilient, with a 3.7% rise, while other capex-related industries posted strong gains. The January recovery was broad-based, with general machinery and production machinery posting strong output gains of 11.7% and 8.1%, respectively. Production of electronic parts and devices also picked up sharply, reaching a post-2013 high with a 10.5% jump (Figure 3).

Manufacturers project a solid production 2.1% gain in February (Figure 4); METI's more reliable projection adjusting for the statistical bias in manufacturers' projections is for a modest 0.4% decline. The METI noted that the survey results are less reliable than usual, as they had not incorporated the im-

part of the mid-February earthquake. That said, as the impact of the semiconductor supply shortage on autos appears to have been smaller than expected thus far, and as we are seeing a broader production recovery supported by strong global capex, we now expect IP to rise 15.5%q/q, saar in 1Q21, followed by an 11.0% gain in 2Q.

Figure 3: Electronic parts and devices

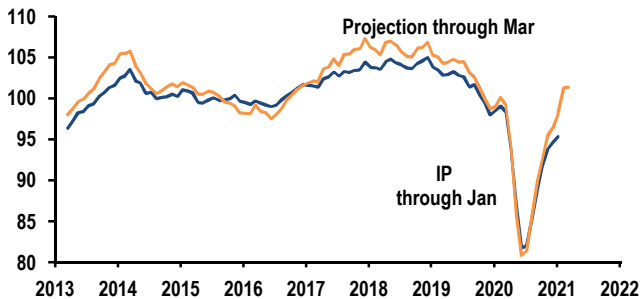
2015=100, sa, both axes



Source: METI, J.P. Morgan

Figure 4: Industrial production and manufacturers' output projection

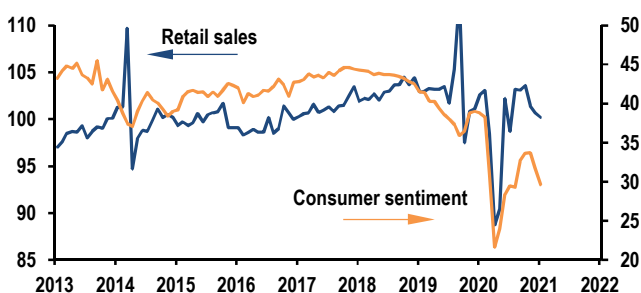
2015=100, sa, 3mma, both axes



Source: METI, J.P. Morgan

Figure 5: Retail sales and consumer sentiment

Index, 2015=100, sa



Source: METI, Cabinet Office, J.P. Morgan

Retail sales fell less than expected

The January retail sales also came out stronger than expected, declining 0.5%*m/m*, sa, against our expectation of a 1.5%*m/m*, sa drop (Figure 5). This was the third consecutive monthly decline, but the pace of decline has moderated since November. Among goods categories, apparel and general merchandise sales posted double-digit declines, reflecting a

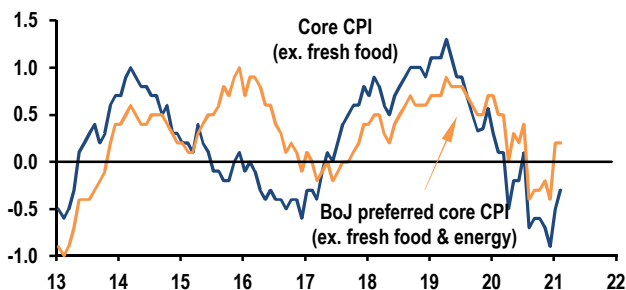
sharp fall in mobility during the New Year holiday shopping season. Although we still expect a large drop in service consumption in January, this milder-than-expected consumption drag in the first month of the renewed state of emergency led us to revise up our GDP-based consumption forecasts to -4.0%*q/q*, saar, from -8.0%.

Goods-services inflation gap widened

In the February Tokyo CPI report, the BoJ's preferred core CPI inflation measure (ex. fresh food and energy) stood at 0.2%*oya*, changed from January but firmer than our expectation for a 0.1%-pt deceleration (Figure 6). Although services prices moderated as expected under the renewed state of emergency, core goods prices picked up with rises in durable goods and food prices, reflecting the firmer-than-expected recovery in domestic demand. Meanwhile, core CPI deflation (ex. fresh food) continued to ease with a smaller drag from energy prices, declining 0.3%*oya* in February after a 0.5% drop in January. In the details of the February Tokyo CPI report, services prices rose 0.1%*oya*, moderating by 0.1%-pt from January. Accommodation fees, which jumped 31%-pts in January due to the temporary suspension of the government's travel subsidy program, which had dragged on core inflation by around 0.5%-pt from August to December, fell 5.1% in February after a 2.1% drop in January. Meanwhile, core goods inflation was firmer than expected, at 0.5%*oya* after a 0.2% print in January.

Figure 6: Tokyo CPI

%oya, excl. the impact of consumption tax rate hike and free education



Source: Statistics Bureau, J.P. Morgan

Data releases and forecasts

Week of March 1 – 5

Tue Mar 2 8:30am	Labor force survey Sa				
		Oct	Nov	Dec	Jan
	Unemployment rate (%)	3.1	2.9	2.9	<u>3.1</u>
	Job offers ratio	1.04	1.06	1.06	<u>1.04</u>

We project that the unemployment rate rose by 0.2%-pt to 3.1% in January, while the job-offers-to-applicants ratio declined by 0.03pt to 1.03. The labor market pressure eased somewhat after the summer, with the government's economic measures supporting temporary increases in job offers. However, as infection cases started to rise since late November and the government renewed the state of emergency in January, we expect the labor market to start deteriorating again.

Tue Mar 2 8:50am	MoF corporate survey %q/q, saar, unless noted, nonfinancial firms				
		1Q20	2Q20	3Q20	4Q20
	Sales	-11.0	-33.7	15.9	
	Current profits	-50.6	-76.2	219.7	
	Capex ex. software	14.3	-26.7	-5.1	
	Capex incl. software (%oya)	0.1	-11.3	-10.6	<u>-2.0</u>

We expect capital expenditures including software in the MoF corporate survey, which is a major input to the second estimate of GDP, fell 2%oya in 4Q20. Capex appears to have recovered in 4Q, based on the result of the other capex indicators such as capital goods shipments and core machinery orders.

Thu Mar 4 2:00pm	Consumer sentiment DI, sa				
		Nov	Dec	Jan	Feb
	Consumer sentiment	33.7	31.8	29.6	<u>32.0</u>
	Standard of living	36.7	34.9	32.2	
	Income growth	35.7	35.0	33.5	
	Labor market conditions	26.5	23.6	21.1	
	Durable goods purchases	35.7	33.8	31.6	

1. The DI asks whether a respondent thinks that now is a good time to purchase durables

We expect consumer sentiment to rise 2.4pts to 32.0 in February, reversing a 2.2pt decline in January. Although the state of emergency was extended through early March, the number of infections has been trending down since late January. We think this led to brighter prospects for economic normalization, raising consumer sentiment in February.

Review of past week's data

Services producer prices (Feb 22)

	Nov	Dec	Jan	
%oya	-0.5	-0.3	—	-0.5
ex. international transportation	-0.4	-0.1		-0.4

The service produce prices index (SPPI) deflation deepened in January reflecting the demand weakness under the renewed state of emergency, falling 0.5%oya after a 0.3% decline in De-

cember. The SPPI deflation had continued to ease in 2H20 after the sharp 2Q decline, but started to deepen again at the turn of the year. For the SPPI, services prices at the producer stage tend to lead to changes in prices at the consumer stage, and therefore we expect a weakening in services consumer prices in the coming months.

Tokyo Consumer prices (Feb 26)

%oya, 2015-based	Nov	Dec	Jan	
Overall	-1.2	-0.5		-0.3
Core (ex fresh food)	-0.9	-0.4	<u>-0.4</u>	-0.3
Ex fresh food and energy	-0.4	0.2	<u>-0.1</u>	0.2

See the main essay.

Industrial production – preliminary (Feb 26)

%m/m, sa	Nov	Dec	Jan	
Production	-0.5	-1.0	<u>-0.5</u>	4.2
Shipments	-1.2	-1.1	<u>3.2</u>	
Inventories	-1.5	1.1	<u>-0.2</u>	
Inventory/shipments ratio	-2.2	2.0	<u>-6.3</u>	

See the main essay.

Commercial sales (Feb 26)

%m/m, sa	Nov	Dec	Jan	
Total retail sales	-2.1	-0.7	<u>-1.4</u>	-0.5
%oya	0.6	-0.4	<u>-3.3</u>	-2.3

See the main essay.

Housing starts (Feb 26)

	Nov	Dec	Jan	
Housing units %oya	-3.7	-9.0	<u>-2.5</u>	-3.1
%m/m, sa	0.7	-4.2	<u>-1.5</u>	2.2
Mn units saar	0.82	0.78		0.08
Floor space, 6mma* (%m/m, sa)	0.6	-0.3		0.1

Housing starts by unit rebounded 2.2%/m, sa in January, after an unexpected sharp decline in December. It remained weak on an oya basis, posting consecutive declines for one year and a half, but the January result suggested it has bottomed. Looking at the details, although built-for-rent has been on downtrend, falling 5.8% in January, the built-for-sale and owner-occupied categories rose firmly at 15.2% and 2.4%, respectively. We expect housing starts by unit to continue to recover even if at a moderate pace, especially in built-for-sale, reflecting the new demand from the increase in WFH. Meanwhile, the six-month moving average of starts by floor space, which we think is a better indicator of real GDP residential investment and in put-in-place terms, edged up 0.1%/m, sa in January, leaving the January level 0.4% annualized above the average in 4Q, when it fell 6.4% ar. Based on this result, we maintain our 1Q forecast for a 5.0% ar rise in GDP-based residential investment.

Source: BoJ, CAO, EJCS, JADA, JCSA, JDSA, JFA, JLM, VMA, Markit, METI, MHLW, MILT, MoF, Reuters, Statistics Bureau, J.P. Morgan forecast

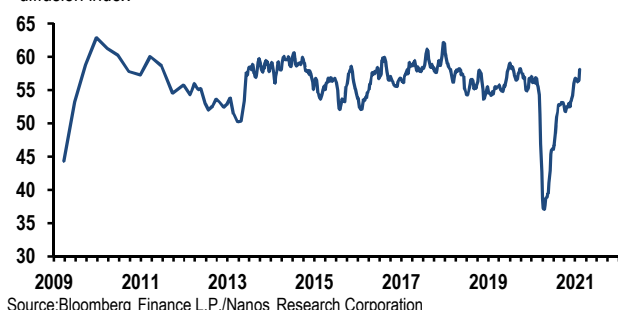
Canada

- **Consumer confidence returned to pre-pandemic levels**
- **Small businesses turned more upbeat**
- **Industrial prices surged in January**
- **BoC Governor Macklem spoke on labor market healing**

The improvement in sentiment indicators stood out this week. Pandemic uncertainty appears to be receding rapidly among consumers and businesses. We expect economic activity will begin to recover starting in March, setting the stage for [a robust rebound](#). We look for 5.2% real GDP growth in 2021 (4Q/4Q) and 2.8% in 2022.

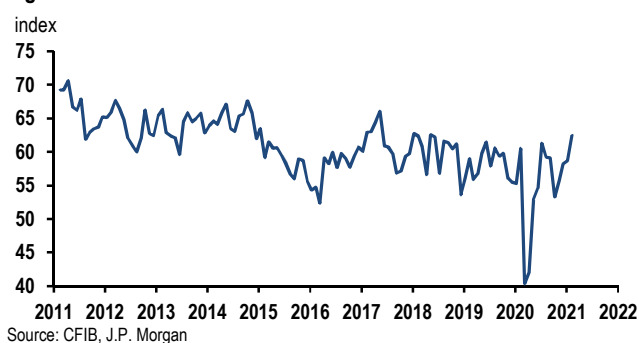
Consumer confidence returned to pre-pandemic levels in the latest survey. Housing outperformance and optimism on the Canadian economy's strength bolstered the positive sentiment. The pocketbook index, based on survey questions on personal finances and job security, and the expectations index both reached 12-month highs (Figure 1).

Figure 1: Economic mood: general survey
diffusion index



Small businesses also turned more upbeat in February as the vaccine roll-out renewed optimism (Figure 2).

Figure 2: CFIB Small business sentiment
index

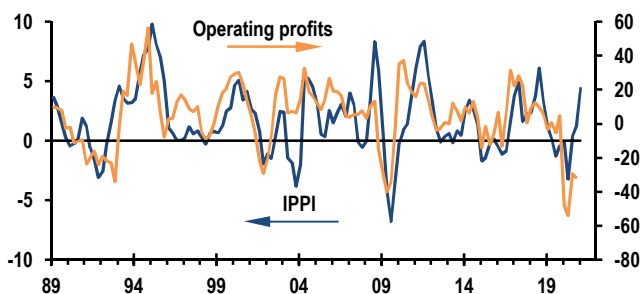


Industrial prices surged in January

The Industrial Product Price Index (IPPI) jumped 2.0% in January, the strongest monthly increase in six years. Among the 21 major product categories, the prices of 15 were up while six were down or unchanged. Prices for lumber and other wood products (+10.8%) were the biggest contributor to the IPPI's increase. Softwood lumber prices have been surging in recent months, and are up over 100% since January 2020 on supply disruptions and tremendous demand for residential building materials. Energy and petroleum product prices climbed for the fourth month in a row in January and chemicals and metals prices also firmed notably. The correlation with consumer prices is generally loose but firming upstream prices support profits (Figure 3). Along with profit gains, we expect favorable business financing conditions will support a capital spending rebound 2021.

Figure 3: Industrial pricing and corporate profits

%oia, both scales



Governor Macklem speaks...

Bank of Canada governor Tiff Macklem spoke this week on the disruptive impact of the pandemic on the labor market. He highlighted that employment is still down more than 850,000 jobs since the start of the pandemic, with the losses disproportionately concentrated among low-wage workers, largely women and younger workers. He was confident that once Canada achieves widespread vaccination, high-contact service industries should be able to resume something approaching full operations, resulting in strong job growth. Governor Macklem made it clear that a healthy labor market was central to achieving the Bank's mandated goal of inflation sustainably at the 2% target. With a complete recovery still a long way off, Governor Macklem clearly signaled that the Bank remains committed to the forward guidance in place since last July. The Bank will keep the policy interest rate at the effective lower bound until economic slack is absorbed so that the inflation target is sustainably achieved. In the Bank's base case projections, that occurs in 2023. And as the governor noted, "we have backed up this commitment with our program of large-scale government bond purchases."

Data releases and forecasts

Week of March 1 – 5

Mon	Current account				
Mar 1	C\$ bn, saqr, unless noted				
8:30am		1Q20	2Q20	3Q20	4Q20
	Current account	-13.9	-7.0	-7.5	<u>-7.1</u>
	(% of GDP)	-2.4	-1.4	-1.3	<u>-1.2</u>
	Merchandise	-8.1	-8.2	-8.8	<u>-8.2</u>
	Nonmerchandise	-5.7	1.2	1.3	<u>1.1</u>
Tue	Quarterly GDP				
Mar 2	Sa				
8:30am		1Q20	2Q20	3Q20	4Q20
	Real GDP,%q/q, ar	-7.3	-38.1	40.5	<u>7.6</u>
	%oya	-0.3	-12.5	-5.2	<u>-3.5</u>
Tue	Monthly GDP				
Mar 2	sa				
8:30am		Sep	Oct	Nov	Dec
	Total,%m/m	0.8	0.4	0.7	<u>0.3</u>
	%oya	-3.8	-3.4	-2.8	<u>-2.8</u>
Wed	Building permits				
Mar 3	%m/m, sa, unless as noted				
8:30am		Oct	Nov	Dec	Jan
	Total	-11.9	12.5	-4.1	<u>7.0</u>
	%oya	-4.4	22.9	3.2	<u>4.4</u>
Fri	International trade				
Mar 5	Sa				
8:30am		Oct	Nov	Dec	Jan
	Balance (C\$ bn)	-3.93	-3.56	-1.67	<u>-1.4</u>
	Exports (%m/m)	2.0	0.0	1.5	<u>2.9</u>
	Imports (%m/m)	1.9	-0.8	-2.3	<u>2.4</u>
	Real balance	-0.79	-0.71	-0.04	
Fri	Ivey PMI				
Mar 5					
10:00am		Nov	Dec	Jan	Feb
	Composite index ¹ (sa)	54.0	51.6	53.0	<u>60.5</u>
	Purchasing index (sa)	52.7	46.7	48.4	<u>61.0</u>

1. Calculated and seasonally adjusted by J.P. Morgan

Review of past week's data

Industrial PPI (Feb 26)

%m/m, nsa, unless noted					
	Nov	Dec	Jan		
Total	-0.5	-1.5	1.7	<u>-1.9</u>	2.0
%oya	0.5	-1.8	2.0	<u>-3.7</u>	4.0
Ex energy	-0.9	-0.9	1.1	<u>-1.4</u>	1.5
%oya	4.0	-4.6	4.8	<u>-6.8</u>	6.1

Source: Statistics Canada, Ivey Business School, CMHC, Markit, Teranet/National Bank of Canada, CREA, CFIB, Bank of Canada, J.P. Morgan forecasts

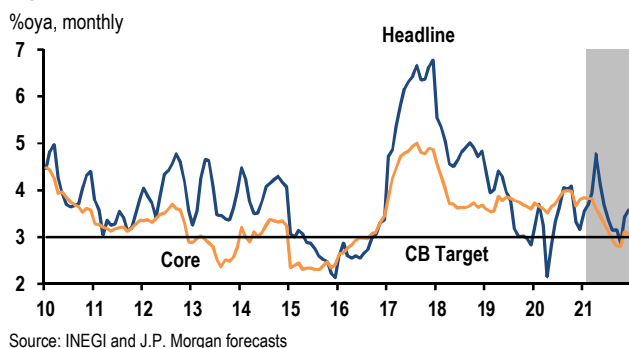
Mexico

- **Minutes suggest more cuts ahead but timing is tricky**
- **With renewed pressures in core goods prices and growth revised up, the space to cut is not wide**
- **We now see inflation at 3.6% this year, from 3.4% and GDP at 5.6% on fiscal stimulus in the US**
- **Next week Banxico's Quarterly Inflation Report in focus**

This week, the minutes of the most recent monetary policy meeting on February 11 when Banxico cut 25bp to 4.0% were pretty much in line with the post-meeting statement. A rich discussion took place on the sources of uncertainty on inflation (e.g. FX dynamics, commodity prices, supply disruptions) and the lingering downside risks to economic activity in the context of fiscal policy inaction during the pandemic. But more importantly, board members seem split about the additional space to cut given financial stability risks and institutional concerns related to recent government decisions—particularly after the government's attempt to alter Banxico's Law and the ongoing discussion to modify the energy reform. We still expect the dovish stance to prevail, resulting in two more cuts in March and August, bringing the rate to 3.5%.

A fair share of the discussion focused on justifying the pause at the end of 2020, when the board opted to pause on the back of lingering inflationary pressures (inflation peaked at 4.1% in October), and in spite of expected relief related to the Black Friday discounts in mid-November. The cautious stance prevailed again when board members addressed the expected incoming price pressures between late March and June, which should raise inflation back to near 5% (Figure 1).

Figure 1: Inflation outlook



Still, some members underscored that those pressures are expected to be temporary and explained by statistical base effects, which should pave the way for more cuts later on. Some of the hawkish comments were related to expected exchange

rate pressures in the context of risk-off episodes, rating downgrades, and public finance concerns, and the recent recovery in commodity prices, but overall the board seemed comfortable with the anchoring of inflation expectations and the fact that economic slack will pave the way for further downward inflation adjustments in 2H21, broadly in line with our expectations.

Governor Diaz de Leon apparently remains firm in stressing the importance of orderly adjustments in the term-structure of interest rates and the relevance of external financing, which in our view suggests he won't favor additional cuts soon—particularly given recent market dynamics. To be fair, we are perplexed that the vote in February was 5-0 given the cautious tone of two members who underscored financial stability concerns, the decreasing growth benefits of additional rate cuts, and the importance of strengthening the credibility of the central bank in reaching its 3% long-term inflation target.

We believe Banxico will cut rates again in March and August, provided inflation behaves as expected, and in spite of our recent upward macroeconomic revisions. Short-term pressures related to higher energy prices will result in a tighter monetary policy decision next month, and if core prices do not budge at the start of 2H, then the pause could extend beyond August, but in the end, we believe a predominantly dovish board and a significant negative output gap will prevail, resulting in rates reaching 3.5% by year-end.

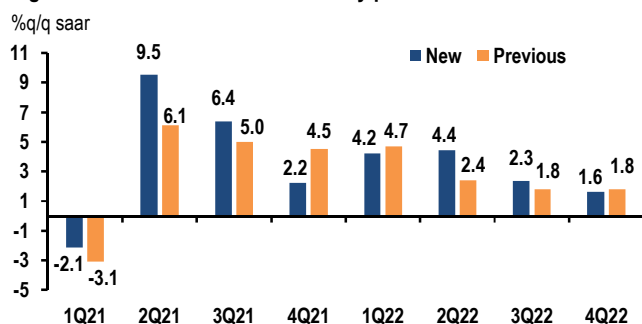
Growth to gain pace on US stimulus...

This week 4Q growth was revised higher to 13.7% ar from 12.9% in the flash estimate. As suspected, the revision leaned mostly on IP (up 16.4% now vs. 13.9%), although services growth was also nudged higher (13.4%). The overarching dynamics throughout the 2H20 recovery remained the same: sectors linked to external demand recovered promptly while domestically-driven sectors lagged. In fact, GDP data for December reinforced this trend, as services linked to domestic demand edged lower for the third consecutive month, contracting 0.2%/m, whereas services related to external demand continued to expand rapidly. Still, the domestic drag remained such that GDP contracted 8.2%/y in 2020.

These trends were already set to intensify early this year, as manufacturing held up against the backdrop of weak services due to renewed lockdowns through mid-February. The drag on manufacturing from gas supply shortages from the US would have deepened the expected GDP contraction in 1Q, but not affected the broad narrative. However, last week our US colleagues raised their GDP forecast over the next several quarters sharply, having incorporated stronger 1Q data and, more importantly, a much larger fiscal stimulus.

Hence, we revise our GDP profile higher, though not without accounting for some domestic nuances. Among these is the fact that we still expect GDP to contract this quarter, even if less than before (-2.1% ar vs. -3.1%). State-level lockdowns and, more recently, a gas shortage for industry largely are behind our grim expectations. That said, thereafter we expect a swift recovery in activity on strong manufacturing and related services (Figure 2).

Figure 2: Real GDP outlook - Quarterly profile



Source: J.P. Morgan forecasts

The updated outlook implies that GDP would move back above its pre-pandemic mark by 1Q22, not around 3Q22, as we thought before. All said, our full-year forecasts for GDP growth now stand at 5.6%/y for 2021, up from 5.1%, and 4.1% for 2022, from 3.7%. While a most welcome boost to our expectations, the thrust from stronger external demand does little to change our medium-term view. We continue to think that domestic demand will remain sluggish, even if recovering faster in 2022 as vaccines become more widespread. This outlook builds on our view that households' and firms' balance sheets have suffered long-lasting damage from the pandemic, particularly amid lack of forceful fiscal support domestically. Legislation that will likely limit competition in some sectors has been a recurrent topic lately, which should add to already strong headwinds to business spending.

... and some unpleasant CPI pressures

We had pointed out that ample slack should lower core inflation throughout this year, and we still believe it will. However, nonfood goods prices have been under pressure for some months now on supply disruptions, and, very likely, continued shifts in demand away from services and toward goods. If we add an even stronger outlook for goods vs. services demand and a narrower output gap, we think risks are sufficient to expect this core component to remain under pressure. We thus raise our core inflation forecast modestly to 3.1%oya from 3.0%, and headline inflation to 3.6% from 3.4%—the latter also takes into account the likelihood of sustained pressure on energy prices (Figure 1). Next week Banxico's Quarterly Inflation Report will probably unveil updated forecasts in the same direction.

Data releases and forecasts

Week of March 1 – 5

Mon	IMEF PMI survey				
Mar 1	Index, sa				
1:00pm		Nov	Dec	Jan	Feb
	Manufacturing	49.0	48.8	50.2	<u>48.9</u>
	Non-manufacturing	49.0	48.0	47.6	<u>46.6</u>
Mon	Remittances				
Mar 1		Oct	Nov	Dec	Jan
7:00am	Total (US\$ bn)	3.6	3.4	3.7	<u>3.0</u>
	%oya	14.1	15.6	17.4	<u>13.7</u>
Fri	Gross fixed investment				
Mar 5	%oya				
7:00am		Sep	Oct	Nov	Dec
	Total	-16.0	-14.6	-12.1	<u>-11.0</u>
	M&Eq	-12.7	-16.9	-14.8	<u>-7.8</u>
	Construction	-18.4	-12.6	-9.9	<u>-13.4</u>

Review of past week's data

Retail sales		Oct	Nov	Dec	
%oya		-7.1	-5.1	<u>-5.2</u>	-5.9
%m/m sa		-0.3	3.6	<u>-1.3</u>	-2.4
Consumer prices					
	Jan 1H	Jan 2H	Feb 1H		
%2w/2w	0.51	0.50	<u>0.12</u>	0.23	
Core	0.24	0.17	<u>0.14</u>	0.22	
%oya	3.33	3.74	<u>3.73</u>	3.84	
Core	3.83	3.84	<u>3.76</u>	3.84	
Labor market report					
% of labor force					
	Nov	Dec	Jan		
Unemp. rate	4.4	3.8	—	4.7	
sa	4.5	4.4	—	4.5	
Economic activity index (IGAE)					
%oya, unless noted					
	Oct	Nov	Dec		
%oya	-5.3	-3.9	<u>-2.5</u>	-2.7	
%m/m sa	1.2	0.9	0.1		
Trade balance					
	Nov	Dec	Jan		
Balance (US\$ mn)	3.0	6.3	<u>-0.6</u>	-1.2	
Exports (US\$ bn)	38.3	43.2	<u>35.7</u>	32.7	
%oya	2.3	11.5	<u>6.2</u>	-2.6	
Imports (US\$ bn)	35.3	36.9	<u>36.2</u>	33.9	
%oya	-3.9	3.7	<u>0.5</u>	-5.9	

Source: INEGI, Banxico and J.P. Morgan forecasts

Brazil

- Policy uncertainty has increased and local markets weakened due to local factors, tighter global conditions
- We thus now call for a 50bp hike in the next meeting with rates reaching 6% in the next year
- Stronger global growth and less fiscal tightening lift our 2021 GDP growth forecast to 3.1%, but financial tightening lowered our 2022 projection to 2.4%
- We also revised up the Dec 2021 IPCA inflation forecast to 4.3% on higher commodity prices

This week we changed our outlook significantly, particularly because uncertainty over economic policy management increased substantially. Following discussions of fuel prices increases and threats of a truckers' strike, President Bolsonaro affirmed on Friday night that the CEO of Petrobras, Roberto Castello Branco, would be replaced by retired General Joaquim Silva e Luna. In addition, the president said over the weekend that more changes should come, possibly in the electricity sector (see "Bolsonaro sinaliza mudanças no governo," *Correio Braziliense*, February 21, 2021). These announcements spilled over in the macroeconomic outlook by raising financial stability concerns.

To contain the market sell-off, the government and Congress accelerated the discussion of the emergency bill. The [draft of the bill released this week](#) was relatively more positive with rules aiming to secure debt sustainability, but no expenditure cuts in the short term and including the renewal of emergency aid. The bill was scheduled to be voted on this week, but disagreements over the minimum level of spending on health and education postponed the vote (see "Senadores querem negociar e votação de PEC emergencial pode ser adiada," *Valor Econômico*, February 24, 2021). The government also sent bills to Congress to initiate the privatization of Eletrobras and the Correios public companies, but the weakening of the local markets continued given the political dynamics and the change in global financial conditions (see "Bolsonaro entrega ao Congresso projeto para privatizar os Correios," *O Globo*, February 24, 2021).

Even after last week's revision to our monetary policy call due to the adoption of the new cash transfers, the recent turbulence—which increased uncertainty over domestic policy—and the tightening in global financial conditions prompted us to now call for a 50bp hike at the [March COPOM meeting](#). This should be followed by similar increases at the coming meetings until the SELIC rate ends 2021 at 5.50% and two final 25bp hikes in early 2022 leaving our terminal SELIC rate at 6%.

While policy uncertainty and tighter financial conditions should contain the economic recovery in the medium term, we think that GDP growth will be stronger this year. Global growth should be stronger than we projected when we last revised our Brazil GDP prospects, and the reintroduction of the emergency aid, which we expect to infuse BRL40 billion into the economy from April to July, is likely to boost household consumption. We now see [GDP growing 3.1% in 2021](#), up from 2.6% previously expected, and 2.4% in the next, down from 2.9% before (Table 1).

Table 1: Annual GDP forecasts

Items	Weight (%)	2019	2020	2021	2022
GDP	100	1.4	-4.3	3.1	2.4
<i>Demand components:</i>					
Private consumption	64	2.2	-5.4	4.5	3.0
Government consumption	20	-0.4	-5.0	-2.5	-0.8
Investment	15	3.4	-3.0	3.8	2.0
Exports	15	-2.4	-1.6	5.0	5.0
Imports	-14	1.1	-9.9	6.0	4.3

Source: IBGE and J.P. Morgan forecasts

We also [revised our IPCA inflation forecasts again](#). Last week, with the introduction of the emergency aid in our outlook, we expected increased inflationary pressures due to more heated demand. This week, the February IPCA-15 suggested a higher starting point for food, fuel, and other goods prices, and we think that the most recent acceleration in commodity prices could increase upward pressure on consumer prices in Brazil. Petrobras increased gasoline prices by more than 10%, which alone raises our IPCA forecast by +10bp, and the gap between domestic gasoline prices and international prices still stands at 7% by our calculations. In addition, after stabilizing briefly, agricultural commodity prices are accelerating again. Taking these factors together, we now look for the IPCA to rise 4.3% this year, up from 4.0% previously, with higher inflation particularly concentrated in the first half of this year. The revisions lifted our core IPCA inflation projection from 3.0% to 3.1% (Table 2).

Table 2: Consumer prices (IPCA)

Components	Weights (%)	2019	2020	2021	2022
IPCA headline	100.0	4.3	4.5	4.3	3.5
BCB core	-	3.2	2.8	3.1	3.1
Administered	25.7	5.5	2.6	7.4	4.4
Market driven prices	74.3	3.9	5.2	3.3	3.1
Goods	38.2	4.2	8.7	3.7	2.6
Non-durable	22.4	6.7	13.2	5.1	3.5
Semi-durable	5.7	0.6	-0.2	1.7	2.2
Durable	10.0	0.0	4.5	1.7	0.7
Services	36.2	3.5	1.7	2.8	3.7
Cyclical services	24.3	3.4	1.7	3.0	3.7
Trend services	11.8	3.9	1.9	2.3	3.8

Source: IBGE and J.P. Morgan forecasts.

With those changes, we lowered our CAD and net FDI inflow forecasts further. We now forecast the CAD this year at US\$4bn (0.2% of GDP) from US\$7bn (0.5%) previously and in 2022 at US\$10bn (0.7% of GDP) from US\$14bn. Also, the recent increase in uncertainty should reduce net FDI inflows, so we trimmed our forecast for 2021 to US\$49bn from US\$55bn and for 2022 to US\$55bn from US\$67bn. These new estimates remain above the CAD and should be augmented by net portfolio inflows, which we now see at US\$16bn this year vs. US\$9bn previously.

On the fiscal front, we now see this year's primary deficit at 2.9% of GDP from 3.2% previously and we now project end-2021 gross debt at 90.3% of GDP, the down from 90.5%. Of note, we continue to assume that BNDES will make an early payment of BRL100bn (1.2% of GDP) to the Treasury before the end of the year.

IPCA-15 slightly higher than we expected

The February IPCA-15 report showed some moderation in headline and core inflation, but overall both remained relatively high. The IPCA-15 increased 0.48%/m/m, slightly below consensus, but more than we thought (0.43%), and the core metric increased 0.46%, 4bp more than we expected. As a result, IPCA-15 inflation is now running at 4.6%oya and core inflation jumped 30bp to 3.1%, the first reading above 3% since March last year. Sequentially, this means a small deceleration in core prices, but they have risen solidly since at least October.

January data suggest lower CAD this year

The CAD came in at US\$7.3bn in January, taking the 12-month deficit down to US\$9.4bn (0.7% of GDP) from US\$12.5bn in December. Meanwhile, foreign direct investment (FDI) disappointed again with net inflows of US\$1.8bn last month, pulling down the 12-month sum to US\$33.4bn (2.3% of GDP) from US\$34.2bn in December. Portfolio investment registered net inflows of US\$4.9bn, led by equities and reducing the 12-month deficit to US\$1.1bn from US\$2.6bn in December.

Credit started 2021 relatively well, but indebtedness keeps growing

Outstanding credit grew 1.1%/m/m, sa (our seasonal adjustment) in January, slightly more than the 0.8% increase in December albeit slower than what was observed through most of 2H20 (an average of 1.5%). Lending rates jumped 1.6%-pts due to seasonal and specific effects while delinquency rates remained historically low. The downside of the release was once again households' indebtedness. Household debt continued to grow in November and reached a new all-time high of 55% of disposable income.

Employment recovering slowly in Dec

The December unemployment rate was 13.9%, a tenth below the consensus, but matching our forecast. Seasonally adjusted, the unemployment rate was stable at 14.7%. By any metric, employment continued to recover only slowly in December, but the number of employed was still 9% short of the pre-crisis level. Average real wages fell for the third month in a row and real labor income (excluding the emergency aid) is still 6% below the pre-crisis level.

Data releases and forecasts

Week of March 1 – 5

Wed	Gross domestic product	1Q20	2Q20	3Q20	4Q20
Mar 3					
7:00am	%q/q, saar	-6.0	-33.2	34.6	<u>10.0</u>
	%oya, nsa	-0.3	-10.9	-3.9	<u>-2.0</u>

Fri	Industrial production	Oct	Nov	Dec	Jan
Mar 5					
7:00am	%m/m, sa	1.0	1.1	0.9	<u>0.0</u>
	%oya, nsa	0.3	2.6	8.3	<u>1.2</u>

Review of past week's data

Consumer prices (IPCA-15)

	Dec	Jan	Feb	
%m/m	1.06	0.78	<u>0.43</u>	0.48
%oya	4.23	4.30	<u>4.52</u>	4.57

Current account balance

	Nov	Dec	Jan	
Current account (CA)	0.1	-5.3	<u>-7.5</u>	-7.3
CA, 12-month sum	-11.8	-12.5	<u>-9.7</u>	-9.4
CA, 12-month sum, %GDP	-0.8	-0.9	<u>-0.7</u>	
Foreign direct investment	1.5	0.7	<u>3.0</u>	1.8

Wholesale prices (IGP-M)

	Dec	Jan	Feb	
%m/m	0.96	2.58	<u>2.46</u>	2.53
%oya	23.14	25.71	<u>28.86</u>	28.94

National unemployment rate

	Oct	Nov	Dec
Rate, 3-month average (nsa)	14.3	14.1	13.9

Fiscal sector

BRL bn, Minus denotes surplus

	Nov	Dec	Jan	
Primary	18.1	51.8	<u>-54.4</u>	-58.4
12-month sum, as % of GDP				
Primary	9.0	9.5	9.5	
Nominal	13.2	13.7	<u>13.8</u>	13.7
Net debt, % of GDP	61.7	63.0	<u>64.8</u>	61.6

Source: BCB, FGV, IBGE, and J.P. Morgan forecasts

Argentina

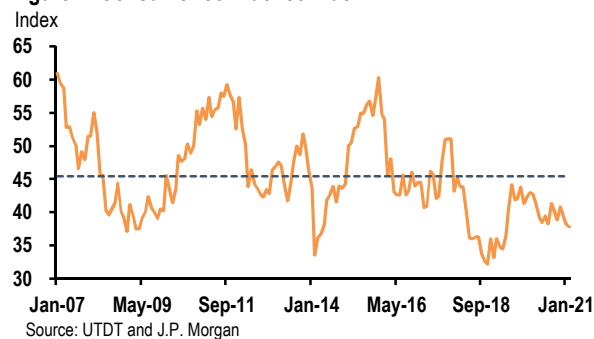
- **Political and consumer sentiment indicators weakened**
- **A lower-than-expected primary surplus in January**
- **We see room for the primary deficit to fall to 3.8%-4.0% of GDP, but risks abound**

The week was marked by a political scandal associated with the vaccine rollout, domestically labeled “vaccine-gate,” which prompted Health Minister Gonzalez Garcia to resign after it became public that he allowed several political leaders, public officials, and family members, as well as friends and businessmen to get vaccinated against rollout protocols. President Fernandez tried to downplay the issue to preserve the government’s image heading into the October legislative elections. Yet, a survey from political consultant Management & Fit showed that 61% of respondents distrust the way the government is dealing with vaccination. Government forward-looking political indicators are already on a downward trend, and the recent scandal is expected to inflict further pain.

Another event with potential political impact was the jail sentence for money laundering handed down to a businessman with close ties to Vice-President Kirchner. The ruling may renew tensions within the government coalition, which could impact the strategy pursued in negotiations with the IMF for a new program. The latest news suggests Argentinean delegates will visit the IMF by mid-March, but there is no official confirmation of the date of an IMF Staff mission yet.

Against this backdrop, it should come as no surprise that the consumer confidence slipped again in February, the third consecutive monthly drop to be down 12% from pre-pandemic levels (Figure 1).

Figure 1: Consumer confidence index



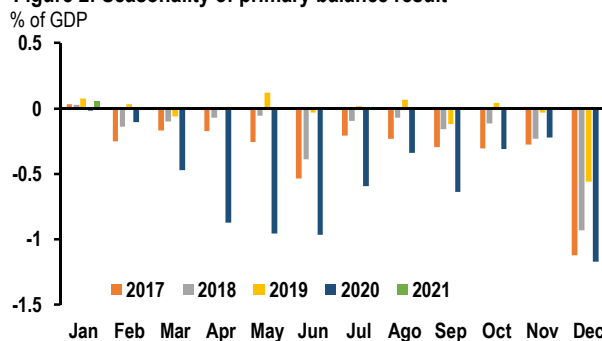
We flag that the deterioration in political and economic sentiment indicators could embolden government efforts to increase spending on consumption, adding risks to our fiscal outlook as well as to the ongoing negotiations with the IMF.

A lower-than-expected primary surplus in January

The Treasury reported a primary fiscal surplus of ARS24bn or 0.1% of GDP in January, compared to an ARS3.8bn deficit in same month last year. The overall deficit (including interest payments) printed at ARS3bn (0.0% of GDP, from a 0.4% shortfall in the same period last year).

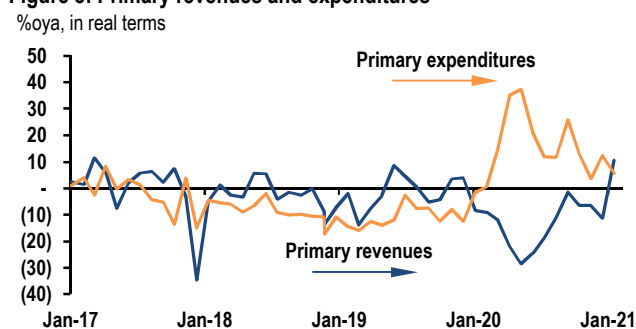
While favored by seasonally lower spending in January (Figure 2), the (cash basis) primary surplus still came in below our expectation and well below the ARS136bn accrued basis result, excluding BCRA transfers, reported by the National Budgetary Office (OPC). The bulk of the difference between the accrued and the cash basis balance is explained by higher-than-expected primary government spending amounting to about ARS160bn, possibly driven by the cancellation of floating debt from the prior fiscal year (estimated at 0.8% of GDP at the end of 2020).

Figure 2: Seasonality of primary balance result



Real primary revenues increased 10.8%oya, interrupting 12 months of consecutive declines (Figure 3). Yet, as we explained [in prior research](#), the firming mainly was driven by higher foreign trade taxes (+90.8%oya, real terms) on delayed export tax collection into January given the oil-seed workers’ strike that paralyzed ports and exports in December.

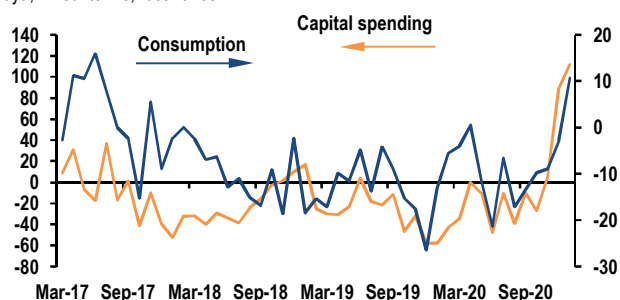
Figure 3: Primary revenues and expenditures



On the other side, real primary spending growth eased to 5.4%oya, from a 9.6% average in 4Q20. Social spending led the deceleration, declining 5.6%oya, mostly on base effects, as the government granted a special bonus to pensioners in January last year. Controlling for this effect, social spending would have declined by 1.7%oya (and real government spending would have increased by 8%oya). Meanwhile, both real consumption and capital spending growth accelerated to 10.7%oya and 112%oya, respectively (Figure 4). Last, economic subsidies decelerated from the strong jump observed in 4Q20 but are still running at a high 33%oya in real terms.

Figure 4: Consumption and capital spending

%oya, in real terms, both axes



Source: Ministry of Treasury and J.P. Morgan

We see room for a reduction in the primary deficit to 3.8%-4.0% of GDP in 2021

We see scope for the government to reduce the primary deficit to 3.8%-4.0% of GDP this year, from 6.5% last year. Yet, the main risks to our forecast include (1) higher COVID-19 spending amid delays in vaccination and a second COVID-19 wave as we enter the winter, (2) lower-than-expected energy tariff adjustments resulting in higher subsidies (note that we are already project a 0.6%-pt of GDP increase in subsidies this year), and (3) a faster-than-expected acceleration in capital and social spending amid the electoral cycle in 2H20.

We continue to flag that any primary deficit above 4% of GDP, absent international market access and additional IFI financing, would put further pressure on BCRA monetary financing and, therefore, on already-high underlying inflation. Our primary deficit forecast is consistent with monetary financing of no more than 2% of GDP, with the remainder of the deficit financed by local markets and (ex.-IMF) multilateral lending. Any monetary financing above the level of seigniorage would compromise the stabilization scenario, exacerbating existing macroeconomic distortions.

Data releases and forecasts

Week of March 1 – 5

Government tax revenues					
Mon		Nov	Dec	Jan	Feb
Mar 1	%oya, real	0.8	1.5	5.0	<u>2.5</u>
Industrial production					
Thu		Oct	Nov	Dec	Jan
Feb 4	%oya	4.9	4.3	-3.1	<u>4.8</u>
Construction					
Thu		Oct	Nov	Dec	Jan
Feb 4	%oya	-0.9	6.2	27.4	<u>28.0</u>

Review of past week's data

Budget balance				
	Nov	Dec	Jan	
ARSbn	-58.6	-307.6	<u>120</u>	24
Economic activity				
	Oct	Nov	Dec	
%m/m	2.1	1.4	<u>1.2</u>	0.9
Trade balance				
	Nov	Dec	Jan	
US\$bn	0.4	-0.3	<u>0.6</u>	1.1

Source: INDEC and J.P. Morgan forecasts

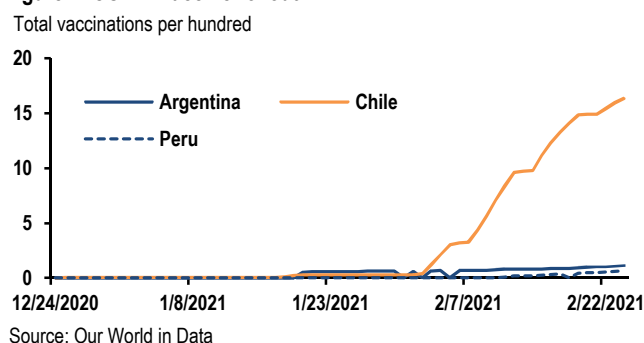
Chile

- We raise 2021 and 2022 GDP growth, by 50bp each
- The efficient vaccine rollout diminishes risks of a third COVID wave and renewed mobility restrictions
- Stronger external demand and higher copper prices also play a positive role
- 2021 and 2022 GDP growth forecasts now at 5.9% and 3.2%, respectively

Vaccines and copper prices vs. political uncertainty

The first weeks of the year have been characterized by growth-positive developments, both domestic and external. On the domestic side, the main positive news has been the availability of vaccines and their rapid rollout, which has situated Chile as a leader in the quest for herd immunity. The government's efforts to close deals for almost twice the vaccines required has allowed the country to move forward much more quickly than peers and even developed economies (Figure 1). While supply risk will linger, the evidence so far suggests risk of a third COVID-19 wave and renewed social mobility restrictions in 2Q21 are easing, which all else equal should be consistent with higher growth in 2Q21.

Figure 1: COVID-vaccine rollout



On the external side, commodity prices in general, and copper prices in particular, have outpaced our commodity analysts' expectations. While our peers remain cautious on the prospects ahead (see [note](#)), the impulse already will boost activity momentum, though likely offset in part by the prevailing institutional uncertainty weighing on capex. As important, copper prices has moved in sync with upward revisions to global economic growth, and growth in Chile's trading partners in particular. To illustrate this point, in just six weeks our house forecast for global growth has been upgraded by 70bp, to 6.1%/y for 2021 and by 30bp to 4.4%/y for 2022. The external demand impulse compounded by the terms of trade windfall is clearly a boost to activity. In all, historical models

suggest that a persistent external impulse will contribute an additional 60-70bp to GDP growth in the next eight quarters, spanning both 2021 and, most important, 2022.

For 2021 annual GDP, we only incorporate 22bp of the 70bp in additional growth coming from the recalibrated external impulse. We thus cautious, assuming political uncertainty will damp the transmission of external demand to domestic demand. Indeed, a copper shock transmits in two main ways. First, the shock to the international price of copper affects the sector's investment decisions, which has implications not only for future mining production but also for the rest of the economy by increasing the demand for the inputs needed to produce the investment goods. Long investment lags in the mining sector makes the shock more persistent but also allow another friction, in this case institutional uncertainty, to have influence the propagation into domestic demand. The second relevant channel is the fiscal one: The country levies royalties and specific taxes on the profits of the foreign-owned mining firms, which further increases the impact of commodity prices in the economy by easing the fiscal budget constraint, allowing higher government spending. We believe this second channel will prove more efficient in propagating the external shock in 2021. In all, we revise 2021 GDP growth by 50bp to 5.9%; 22bp of the upward revision to the 2021 forecast stems from a stronger external impulse, as noted above, while the remaining 28bp owes to the quicker-than-anticipated vaccine rollout.

In 2022 we expect the positive external tailwind to take full effect once the political uncertainty dissipates. Of course, our projection assumes that both the debate on a new Constitution and the election outcome do not create macroeconomic instability. Thus, we raise 2022 GDP growth by additional 50bp, to 3.2%. Of note, we expect growth to decelerate in 2H22 as the external impulse ebbs, and to converge to Chile's potential growth rate, which we believe will be lower than before COVID absent supply-side reforms.

Fiscal accounts to benefit from copper price windfall

Stronger activity together with higher copper prices will reduce the lower fiscal deficit. We lower our headline fiscal deficit forecast, to 3.8% of GDP from 5%. The government is a bit more optimistic, and projects 3.3% of GDP. The main difference in our projections is that we still expect higher expenditures in 2021 at 26.6% of GDP, while the government projects 26.1%. For 2022, our modal scenario is for a 4.4% of GDP deficit, slightly above the official estimate at 4.2%. Following these revisions, we still expect gross debt to trend higher in the coming years, reaching 46.5% of GDP by 2025.

2021 current account revised to -1.6% of GDP (from -2.7%)

We also lower the 2021 current account deficit forecast to 1.6% of GDP. At this stage of the year, there are three key pillars to external accounts. First, higher copper prices. Historical elasticities suggest a 10% persistent copper price increase improves the trade balance by 0.4% of GDP, though the remittance of mining sector profits abroad tempers the impact on the overall current account to 0.27% of GDP.

The second pillar relates to the operational decisions of the mining sector. We expect flattish production for the year, but the risk to our base case appears to be biased downwards as suggested by the decoupling between copper exports in value and prices. On the financial side, it would be very important how the decision about profit remittance abroad evolves in the coming quarters, particularly in the second half of the year. We have argued that institutional and political uncertainty delays reinvestment, which would prompt a larger outflow in the current account.

Finally, the third pillar relates to the recovery in imports associated with the activity rebound and also higher oil prices. Note that merchandise imports (FOB) collapsed by US\$10.6bn in 2020, of which US\$3.6bn was explained by energy. We project oil prices to increase 42%/y in 2021, which would add about US\$4.3bn in energy imports to US\$11.1bn.

Chile

Data releases and forecasts

Week of March 1 - 5

Economic activity					
Mon		Oct	Nov	Dec	Jan
Mar 1	%oya	-1.2	0.3	-0.4	<u>-1.5</u>

IMCE Business confidence					
Mon-Fri		Nov	Dec	Jan	Feb
Mar 1-5	Index	54.2	48.0	54.4	56

Nominal wages					
Fri		Oct	Nov	Dec	Jan
Mar 5	%oya	4.0	4.6	4.0	<u>4.0</u>

Review of past week's data

Unemployment				
	Nov	Dec	Jan	
%oya	10.8	10.3	<u>10.4</u>	10.2

Retail sales				
	Nov	Dec	Jan	
%oya	25.0	3.4	<u>5.6</u>	5.8

Manufacturing production				
	Nov	Dec	Jan	
%oya	-1.4	0.4	<u>-1.5</u>	-4.4

Source: INE, BCC and J.P. Morgan estimates

Colombia

Data releases and forecasts

Week of March 1 - 5

Exports					
Thu		Oct	Nov	Dec	Jan
Mar 4	\$bn	2.6	2.5	3.0	<u>2.7</u>

CPI					
Fri		Nov	Dec	Jan	Feb
Mar 5	%m/m	-0.15	0.38	0.41	<u>0.42</u>
	%oya	1.49	1.61	1.60	<u>1.34</u>

Review of past week's data

Unemployment rate				
	Nov	Dec	Jan	
%oya	13.3	13.4		17.3

Source: DANE and J.P. Morgan estimates

Peru

Data releases and forecasts

Week of March 1 - 5

GDP					
Mon		1Q20	2Q20	3Q20	4Q20
Feb 22	%oya	-3.5	-30.2	-9.4	<u>-1.9</u>

Review of past week's data

GDP				
	2Q20	3Q20	4Q20	
%oya	-30.2	-9.4	<u>-1.9</u>	-1.7

Source: INEI and J.P. Morgan estimates

United Kingdom

- **Next week's Budget to announce net stimulus**
- **But with a roadmap for fiscal tightening including higher taxes**
- **Unemployment rate still showing a slow rise**

Next week's Budget looks set to contain a mixed bag of extended emergency support with a flavor of the first steps toward fiscal consolidation. We discuss the details of these below, but expect the extended stimulus measures to amount to just under 1% of GDP, lasting three to six months. We have argued for some time that taxes would have to go up this year. That looks increasingly likely to happen, with media reports suggesting the Chancellor will announce corporation tax increases next week. This comes amid speculation of a freeze in the higher-rate income tax threshold and an increase in the capital gains tax.

If implemented next week this would be an even earlier start to tax increases than we had expected. However, we continue to expect the Chancellor to announce and outline the path ahead next week rather than enact a raft of immediate tightening measures at a still-fragile stage in the recovery. A 6%-pt rise in corporation tax, for example, likely would be phased in over the next three years. Other taxes could be hinted at or pre-announced but we continue to think they will not become effective until late this year (at the next Budget) and hence will be more relevant for 2022. This would leave a net fiscal boost for the next six months. Beyond that, the onset of tax increases combining with the expiry of emergency support schemes will deliver a net fiscal drag. We assume net tax hikes worth around 1% starting mostly from later this year.

Given a firmer growth outlook compared to the last fiscal update in November, recent undershoots in the monthly public borrowing figures, and net tax increases from later this year, we expect the OBR will be able to project the deficit returning to nearer to 2.5-3.0% of GDP by the end of its forecasting horizon (vs. 4% previously) and the debt ratio resuming a downward trajectory from 2022 or 2023 (Table 1). The changes are more relevant than the level, which is difficult to forecast to due various methodological treatments. We expect the OBR will use a GDP growth forecast for 2021 that is a little softer than our 5.6%.

In terms of stimulus next week, we have been expecting a giveaway package to include extensions to the job support schemes, the business rates holiday, the supplement to unemployment benefit payments and the cuts to both VAT and stamp duty. We expect the latter two to involve an additional three months of support. But regarding the wage subsidy

schemes we previously estimated that an extension closer to six months would be required to prevent an abrupt spike in job losses, as it will take longer than three months for GDP to normalize. We would only expect the furlough scheme in its current form to be extended by a month or two to the end of June, but at least a watered-down replacement scheme will be needed thereafter. We have assumed the cost of these for the 2021 fiscal year beginning in April will be around £20bn, or just under 1% of GDP. If additional stimulus for 1Q (which would fall into the 2020/21 fiscal year) is included, the overall giveaway package is likely to be closer to £25-30bn.

We argued previously that net tax increases amounting to 1%-2% of GDP would be required for the OBR to project a falling debt ratio again. Where we are in this range next week will depend on how pessimistic the OBR is on the labor market. Last time it expected the unemployment rate to peak at almost 8% this year. This would imply pandemic scarring worth 3% of GDP, which we estimate would necessitate a 2% of GDP fiscal consolidation to get the debt ratio falling again by the end of this parliament. If the OBR instead takes a more optimistic view that the unemployment rate will peak closer to 6.5% (as in our forecast) then expected longer-term scarring might be closer to 2% and would require fiscal consolidation of closer to 1% of GDP to deliver the same objective on debt.

Further increases in public spending are likely for the next couple of years. With another Spending Review due later this year it is not clear that this will be fully acknowledged in next week's Budget. But further sustained increases in public spending that go beyond current plans would need to be matched with further tax increases. That would imply gross tax increases might ultimately exceed the 1% of GDP we mention. Other candidates not already mentioned above are further progress on building up a digital services tax, the introduction of national insurance for the self-employed, and stamp duty and council tax reform. Not all of these will necessarily be needed. But our base view remains that the bulk of these changes will become effective from later this year, even if they are announced next week.

Table 1: Expected OBR fiscal projections: March 2021

% of GDP	20/21	21/22	22/23	23/24	24/25	25/26
Deficit (£bn)	370	154	85	74	69	64
Deficit (%)	17.7	6.7	3.5	2.9	2.6	2.4
Current	13.8	3.9	0.6	0.0	-0.3	-0.4
Investment	3.9	2.8	2.9	2.9	2.9	2.8
Structural	17.0	6.1	3.1	2.7	2.5	2.4
Change	14.4	-10.9	-3.0	-0.4	-0.2	-0.1
Net Debt (ex. BoE)	89.5	90.6	90.9	91.0	90.2	89.5
Net Debt	100.3	102.4	102.1	101.7	96.0	94.2

Source: ONS, J. P. Morgan

Signs of labor market resilience

The labor market remains resilient against a backdrop of tight restrictions. In the latest labor market report, the ILO unemployment rate rose by a tenth to 5.1% over the three months to December, still being contained by heavy use of job subsidy schemes, which are likely to be extended in next week's Budget and therefore will prevent a clearer picture from emerging until the second half of the year. In light of the roadmap for easier restrictions and our expectation of a significant GDP rebound, we think the rise in the unemployment rate later this year will be limited to a 6.0-6.5% peak, although there is still much uncertainty around that estimate. The timelier and more accurate PAYE payroll-based employment measure for January revealed a second consecutive monthly increase, of 0.3%/m/m, which hints that a stronger-than-expected trend is unfolding.

Data releases and forecasts

Week of March 1 – 5

Mon	Money supply				
Mar 1	Sa				
9:30am		Oct	Nov	Dec	Jan
	M4 ex IOFCs (%m/m)	1.4	1.3	0.5	
	M4 ex IOFCs (%3m/3m, ar)	7.6	13.3	13.7	
	M4 (%m/m)	0.7	0.8	0.7	
	M4 (%oya)	13.0	12.9	13.4	
	M4 lending (%m/m) ¹	-0.2	0.8	0.2	
	M4 lending (%oya) ¹	3.8	4.2	3.9	

¹: Excludes the effect of securitization.

Mon	Net lending to individuals (BoE release)				
Mar 1	£ bn, average				
9:30am		Oct	Nov	Dec	Jan
	Consumer credit (ch, m/m)	-0.6	-1.5	-1.0	
	Mortgage approvals (000s, sa)	98.2	105.3	103.4	
	Secured lending (ch, m/m)	4.6	5.7	5.6	

Mon	PMI survey final, manufacturing				
Mar 1	% balance, sa				
9:30am		Nov	Dec	Jan	Feb
	Overall index	55.6	57.5	54.1	
	Output	56.7	55.9	50.7	

Wed	PMI survey final, services & composite				
Mar 3	% balance, sa				
9:30am		Nov	Dec	Jan	Feb
	Services business activity	47.6	49.4	39.5	
	Composite				
	Output	49.0	50.4	41.2	
	New orders	48.9	49.8	44.1	
	Employment	42.3	47.2	45.5	

Thu	New car registrations				
Mar 4	%3m/12m nsa				
9:00am		Nov	Dec	Jan	Feb
	Total	-9.4	-13.7	-26.0	-
	Private (ex. bus. and fleet)	-7.8	-15.7	-28.8	-

Thu	PMI survey final, construction				
Mar 4	% balance, sa				
9:30am		Nov	Dec	Jan	Feb
	Overall index	54.7	54.6	49.2	-
Fri	Trade balance				
Mar 5	£bn, sa				
9:30am		Oct	Nov	Dec	Jan
	Total	-4.7	-6.6	-6.2	
	Goods	-13.3	-14.8	-14.3	
	Services	8.6	8.2	8.1	
Fri	Halifax house price index				
Mar 5	Sa				
8:30am		Nov	Dec	Jan	Feb
	%m/m	1.0	0.0	-0.3	
	%oya	7.5	5.8	5.3	
	%3m/3m saar	16.0	10.6	6.5	

Review of past week's data

Labor market statistics

Sa					
	Average weekly earnings (3mma %oya sa)				
		Oct	Nov	Dec	
	Headline	2.8	3.6	3.7	4.7
	Ex bonuses	2.8	3.6		4.1
	Private sector ex bonuses	2.5	3.4	3.3	4.0
	Labor force survey (all percentage rates, sa)				
	Three months to:	Oct	Nov	Dec	
	Activity rate	63.8	63.8		63.6
	Employment rate	60.6	60.6		60.3
	Unemployment rate	4.9	5.0	5.2	5.1
	- single month	5.2	5.0	5.2	5.1
	Change over three months to:	Oct	Nov	Dec	
	Employment (000s)	-143	-88	=	-114

CBI distributive trades

% balance		3Q20	4Q20	1Q21
	Avg. selling prices expected	7	16	33
	Total employment expected	-23	-52	-31
	Investment intentions (next year)	-32	-12	-8
	Business situation (next 6 mths)	7	-19	-2

CBI survey of services sector

% balance		3Q20	4Q20	1Q21
	Bus. and prof services	-32.0	-21.0	-21.0
	Consumer services	-64.0	-42.0	-76.0

Source: Rightmove, CBI, BBA, BCC, GFK, BRC Markit, SMMT, RICS, Land Registry, ONS, BoE, and J.P. Morgan forecasts

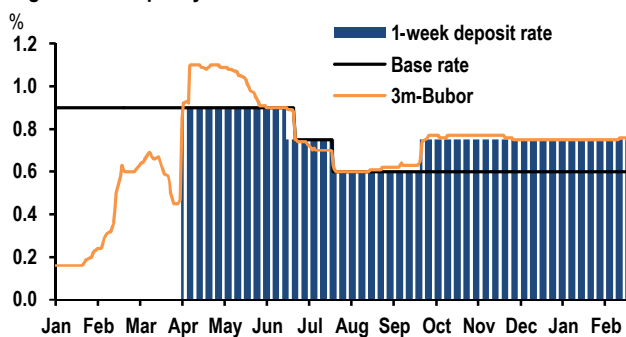
Emerging Europe

- **Hungary: NBH maintained its cautious stance**
- **Turkey: CBRT tightened policy further with an RRR hike**

Hungary: NBH stays in wait-and-see mode

As anticipated, Hungary's Monetary Council kept the base rate unchanged at 0.6% (Figure 1), with no changes to the interest rate corridor setup (o/n depo at -0.05%, o/n lending at 1.85%). The key 1-week deposit facility rate is set every Thursday, but there were no hints of any upcoming changes. In the statement, the NBH reiterated the decision to shift liquidity injections toward QE and away from LT repo, indicating it will maintain a flexible approach and a lasting presence in the market, partially with the objective of supporting the lengthening of the government's debt maturity profile.

Figure 1: NBH policy rates and market rates



Source: NBH

In recent weeks, on the back of rising DM yields, growing concerns over inflation, and perceived hawkishness from the NBH, markets began pricing imminent hikes in Hungary. Yet, the NBH's statement revealed no change in stance, repeating the same cautious, hawkish-leaning tone of recent months, but again, without any hint of matching that with action. The central bank sees inflation somewhat above its 3% oya target in 2021 (3.5%-3.6%) and returning to target next year, but highlighted the need to be particularly cautious. This is due to more uncertain pricing behavior and to expected near-term CPI volatility, on the back of base effects and tax changes. In particular, the NBH is concerned with a potential shift in market sentiment toward EM, which it considers the greatest inflation risk (via currency depreciation). Therefore, the NBH said it was ready to sustain a gap between the base rate (0.6%) and the 1-week deposit facility rate (0.75%) for as long as inflation risks warranted.

Against this background, even with core CPI inflation converging to the target, Hungary's elevated CPI path together with the NBH's sizable liquidity injections stands out. This could easily

trigger a turn of market sentiment with the forint underperforming its peers as it did in 2020. The window we previously saw for the NBH to lower the 1-week deposit facility rate toward the base rate level has therefore most likely closed, and we see the central bank cautiously aiming to keep the current setup as is. Hungary has a relatively high policy rate in the regional context and the current account has returned to surplus, so the forint is somewhat better anchored than last year. Nonetheless, as core CPI inflation re-accelerates in 2022, we see increasing pressure for the NBH to tighten policy. If liquidity injections proceed at the current pace for a long time, or core inflation surprises to the upside, the pressure to tighten could escalate.

Turkey: CBRT tightens further

After the cumulative 675bp increase in the policy rate in the last months of 2020, the CBRT continued tightening financial conditions, this time with an RRR hike. The CBRT raised the TRY reserve requirement ratio by 200bp for all liability types and all maturities. The Bank also lowered the upper limit on the use of foreign currency and gold for TRY reserve requirements in the ROM system. These measures will likely lead to a TRY25 billion increase in the TRY reserve requirements. Interestingly, this was not a reaction to the lira weakening in recent days but was discussed in the MPC meeting last week. According to the minutes, the MPC members believed that "the decelerating impact of the strong monetary tightening on credit and domestic demand is expected to become more significant; hence the effects of demand and cost factors on inflation are envisaged to wane gradually." But they were also wary of the risks associated with rising global commodity prices and still-robust domestic demand. Regarding the domestic demand, members were nervous about the recent fall in loan and deposit rates and the recovery of lending to individuals. The MPC minutes explicitly underlined the need for a RRR hike. Also importantly, the members emphasized that "the policy rate is the sole instrument to determine the monetary policy stance, while the required reserve ratio is a tool that affects the transmission of the monetary stance determined by the policy rate to deposit, loan and other money markets." This could relieve concerns that the CBRT would use RRR hikes as a stealthy way of monetary tightening as it has done in the past.

Data releases and forecasts

Week of February 22 – 26

Czech Republic:

Mon Mar 1 9:00am	PMI Index	Nov 53.9	Dec 57.0	Jan 57.0	Feb —
	PMI, Manufacturing				
Tue	Real GDP, preliminary				

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Economic Research**Emerging Europe**

February 26, 2021

J.P.Morgan

Mar 2	%oya unless otherwise stated				
9:00am		1Q20	2Q20	3Q20	4Q20
	Real GDP, nsa	-1.9	-10.8	-5.0	<u>-5.1</u>
	%q/q, saar	-12.5	-29.9	30.8	<u>1.2</u>
	Private consumption	0.0	-8.1	-3.9	—
	GFCF	-3.9	-4.9	-11.5	—

Source: CNB, National Statistics, Eurostat, J.P. Morgan forecasts

Hungary:

Tue	Real GDP, final				
Mar 2	%oya, unless otherwise stated				
9:00am		1Q20	2Q20	3Q20	4Q20
	Real GDP	2.2	-13.6	-4.6	<u>-3.7</u>
	%q/q, saar	-1.6	-46.8	54.0	<u>4.5</u>
	Domestic demand	3.9	-6.5	-4.6	—
	Private consumption	4.6	-8.3	-2.7	—
	Fixed investment	-4.1	-10.9	-13.7	—

Thu	Retail trade				
Mar 4	% change				
9:00am		Oct	Nov	Dec	Jan
	%oya wda	-2.0	-0.7	-4.0	—
	%m/m, swda	0.9	1.0	-0.2	—

Thu	External trade, final				
Mar 4	EUR mn				
9:00am		Sep	Oct	Nov	Dec
	Trade balance	1140	895	836	<u>310</u>
	Ytd	3665	4559	5396	<u>5706</u>
	Ytd a year ago	3527	3906	4235	<u>4334</u>
	Exports, %oya	6.1	0.1	7.9	<u>11.8</u>
	Imports, %oya	-0.8	-5.1	2.6	<u>9.2</u>

Thu	NBH 1-week deposit facility rate decision	
Mar 4	%	

On hold: 0.75%

Fri	Industrial output				
Mar 5	%oya				
9:00am		Oct	Nov	Dec	Jan
	Production, wda	2.2	1.5	1.1	—
	Production, nsa	0.2	3.4	5.8	—
	%m/m, swda	2.3	-1.0	-2.4	—

Source: NBH, National Statistics, Eurostat, J.P. Morgan forecasts

Poland:

Mon	PMI				
Mar 1	Index				
9:00am		Nov	Dec	Jan	Feb
	PMI, Manufacturing	50.8	51.7	51.9	—

Wed	NBP rate decision	
Mar 3	%	

On hold: 0.10%

We expect the NBP to keep rates unchanged next week, with the message still leaning on the cautious side macro-wise, signaling risks of a delayed recovery due to the pandemic. The statement should reiterate the intention to continue using the QE program, but under dete-

riorated market sentiment, it's not clear the MPC will keep the phrasing regarding potential new FX interventions. Two days later at the governor's Q&A, we expect Glapinski will keep the message similar to last month's, reiterating the view that rates on hold are the most likely outcome, but with openness to move either way if the circumstances so demand. It will be interesting to see if the issue of rising bond yields is brought up, and if so, whether the governor will signal any intention to fight it through asset purchases.

Source: NBP, National Statistics, Eurostat, Markit, J.P. Morgan forecasts

Romania:

Thu	Retail sales				
Mar 4	%oya				
9:00am		Oct	Nov	Dec	Jan
	Retail sales, sa	5.3	4.8	4.2	—
	%m/m, nsa	1.5	0.5	0.2	—

Source: National Statistics, Eurostat, J.P. Morgan forecasts

Russia:

Mon	PMI surveys				
Mar 1					
10:00am		Nov	Dec	Jan	Feb
	PMI, Manufacturing	46.3	49.7	50.9	<u>52.0</u>
	PMI, Services	48.2	48.0	52.7	<u>54.0</u>

Fri	Consumer prices				
Mar 5	%oya, unless otherwise stated				
4:00pm		Nov	Dec	Jan	Feb
	%oya	4.4	4.9	5.2	<u>5.46</u>
	%m/m, nsa	0.7	0.8	0.7	<u>0.58</u>

Source: Rosstat, MinFin, AEB Russia, Markit, J.P. Morgan forecasts

Turkey:

Mon	Gross domestic product				
Mar 1	%oya, real terms				
10:00am		1Q20	2Q20	3Q20	4Q20
	GDP	4.5	-9.9	6.7	—
	Private Consumption	4.5	-8.8	9.2	—
	Public Consumption	3.2	-2.4	1.1	—
	Capital Formation	-0.3	-6.2	22.5	—
	Exports	0.3	-36.3	-22.4	—
	Imports	21.7	-7.7	15.8	—

Wed	Consumer prices				
Mar 3	% change				
10:00am		Nov	Dec	Jan	Feb
	Consumer prices				
	%oya	14.0	14.6	15.0	<u>15.2</u>
	%m/m	2.3	1.2	1.7	<u>0.5</u>
	Producer prices				
	%oya	23.1	25.1	26.2	<u>26.5</u>
	%m/m	4.1	2.4	2.7	<u>0.7</u>
	Core CPI (I)				
	%oya	13.3	14.3	15.5	<u>15.8</u>
	%m/m	2.1	1.0	1.1	<u>0.0</u>

The rise in annual inflation mainly reflects a weak base while the monetary tightening delivered over the last three

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Economic Research**Global Data Watch**

February 26, 2021

J.P.Morgan

months and the lira strength will likely reduce price pressures. We see inflation stable around 15% until May.

Source: Turkstat, CBRT, Ministry of Treasury and Finance, J.P. Morgan forecasts

Review of past week's data**Hungary:****NBH rate decision**

%

NBH held the base rate at 0.60%, as expected. See main text for detail.

NBH 1-week deposit facility rate decision

%

NBH held the 1-week depo rate at 0.75%, as expected.

Average gross wages

%oya

	Oct	Nov	Dec	
Gross wages, nominal	8.8	8.6	—	10.6
Industry	8.7	7.4	—	10.5
Public sector	7.4	8.1	—	7.0

Source: NBH, National Statistics, Eurostat, J.P. Morgan forecasts

Israel:**BOI rate decision**

%

As expected the Bank of Israel kept the policy rate at 0.10% and the forward guidance message unchanged. The statement took a cautiously optimistic tone, citing the successful vaccine rollout and recent economic normalization but remaining wary of virus-related uncertainty. The recent firmer-than-expected 4Q GDP and January CPI data support the on-hold stance with BOI noting that "the inflation environment remains low but continues to trend upward moderately." Little was mentioned about FX following the very large January intervention, except that the resulting ILS weakening will help export performance and the return of inflation to target.

Source: BOI, National Statistics, J.P. Morgan forecasts

Poland:**Real GDP, final**

%oya, unless otherwise stated

	2Q20	3Q20	4Q20
Real GDP	-8.4	-1.5	-2.8
%q/q saar	-31.4	35.5	-2.8
Domestic demand, nsa	-9.9	-3.2	-3.4
Private consumption	-10.8	0.4	-3.2
Fixed investment	-10.7	-9.0	-10.9

Source: NBP, National Statistics, Eurostat, Markit, J.P. Morgan forecasts

Turkey:**Capacity utilization**

%

	Dec	Jan	Feb	
Total manufacturing	75.6	75.4	—	74.9
Durables	73.6	73.8	—	76.8
Nondurable	71.0	70.6	—	70.6

Foreign trade

US\$ bn, except as noted

	Nov	Dec	Jan
Trade balance	-4.6	-4.1	-3.6
Exports	15.3	16.9	14.3
%oya	-1.1	15.5	3.3
Imports	19.8	21.0	17.9
%oya	11.9	10.6	-3.5

Source: Turkstat, CBRT, Ministry of Treasury and Finance, J.P. Morgan forecasts

South Africa & SSA

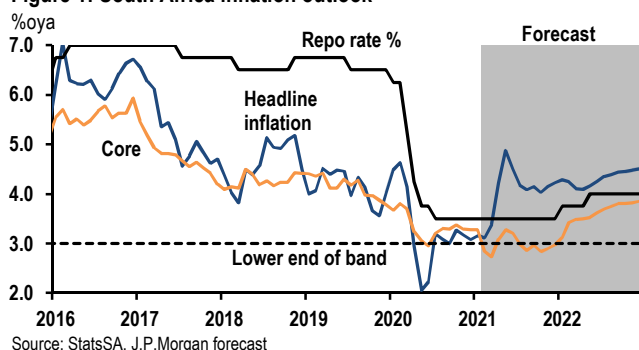
- **South Africa: We raise full-year growth to 4.3%/y/y on improved global backdrop and ToT boost**
- **We add another SARB policy rate hike in 1H22 as the output gap now is seen as somewhat narrower**
- **Budget '21 proposal strikes a balance between the need to support the economy and fiscal consolidation**
- **Treasury projects an improved fiscal trajectory, with debt stabilizing at 88.9% of GDP in FY25**

SA: SARB to begin policy normalization in 1H22 on improved growth momentum

The improved global backdrop, and terms of trade boost, prompted us to mark up our 2021 GDP growth forecast for South Africa to 4.3%/y/y (from 3.3%). Taking our cue from the GDP growth upgrade in the US, we have raised our quarterly GDP profile and also more comprehensively incorporated the consumption boost from higher commodity prices. We now expect GDP to grow 3%/q/q, ar (from no growth previously) in 2Q and 2% (from 1%) in 3Q. Our forecasts for 1Q and 4Q are unchanged at -1.5% and 1.5%, respectively, which takes full-year growth to 4.3%/y/y in 2021.

Our quarterly projection encompasses the recently announced household income support from government, which has been extended by three months to April, and a lesser fiscal drag as tax hikes were withdrawn from the Budget. One downside risk to our more constructive outlook is the possibility of more severe and frequent load shedding. In our forecast we model a few days of stage 2 load-shedding every month this year, with the situation unlikely to improve in the near term.

Figure 1: South Africa inflation outlook



With the improved growth outlook, and a swifter projected narrowing of the output gap, we expect the SARB to hike the policy rate twice next year. This includes an additional hike compared to our earlier predicted policy rate path. While the steady ZAR in recent weeks reduces risks of a near-term hike

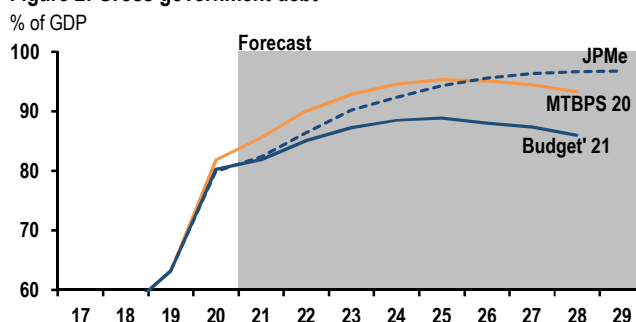
the likely output gap revision should prompt the SARB QPM model to signal a total of 75bp in tightening by end-2021. Even so, we expect the SARB to under-deliver relative to the QPM model projections as long as USD/ZAR remains well below 15.50. We therefore expect the SARB to begin its tightening cycle with a 25bp hike in 1Q22 and a further hike in 2Q22 (Figure 1).

Budget '21 signals an improved fiscal outlook with debt ratio stabilizing in 2025

We believe the Budget '21 proposal presented this week successfully navigated the trade-off between extending further short-term social relief and embarking on the required medium-term structural fiscal reform. The near-term fiscal outlook improved as reflected in a 1.1%-pt upward revision to the fiscal balance in FY21-23 and we see scope for 0.6%-pt of GDP further revenue upside in FY21. Treasury now projects a 9% of GDP main budget fiscal deficit in FY21 (from 10.1% in the MTBPS) and 7.4% in FY22 (from 8.6%) after a likely 12.3% shortfall in FY20. Treasury's revised tax-to-GDP ratio very closely matches our expectation when we utilize a relatively conservative terms-of-trade scenario and pragmatic input assumptions. We see scope for marginally higher nominal GDP growth and potential second-round gains from the terms-of-trade to boost revenue by a further 0.6%-pt of GDP in FY21 and 0.4%-pt in FY22 with risks to FY23 receipts broadly balanced.

Treasury projects an improved medium-term debt profile with the debt-to-GDP ratio almost 5%-pts lower in coming years and debt stabilizing at 88.9% of GDP in FY25 (Figure 2). Near-term gross debt dynamics have undoubtedly improved related to MTBPS projections. Yet, we estimate that debt stabilization would require a 2.2% of GDP primary surplus (corresponding to a 4.7% fiscal deficit), which seems higher than what Treasury implicitly uses in its long-term projection, perhaps due to our lower potential growth and higher stock-flow adjustment assumptions. We expect debt stabilization only in FY27 rather than the FY25 incorporated into the Budget projections.

Figure 2: Gross government debt



South Africa

Data releases and forecasts

Week of March 1 – 5

Mon Mar 1	New vehicle sales %oya, except as noted				
		Nov	Dec	Jan	Feb
	Total vehicle sales	-12.5	-10.6	-14.3	—
	%m/m nsa	1.0	-4.7	-7.0	—
Mon Mar 1 11:00am	Barclays BER PMI Index				
		Nov	Dec	Jan	Feb
	PMI (% weights)	52.6	50.3	50.9	—
	Business activity (25)	52.2	44.9	43.5	—
	New sales orders (30)	49.0	45.2	47.2	—
Fri Mar 5 8:00am	SARB official reserves US\$ bn, except noted				
		Nov	Dec	Jan	Feb
	Gross reserves (R bn)	821.1	807.6	822.3	—
	Gross reserves	53.8	55.0	54.8	—
	International liquidity	51.3	52.1	52.0	—

Review of past week's data

Zambia : CPI

%oya	Dec	Jan	Feb	
	19.2	21.5	—	22.5

Source: Haver, J.P. Morgan forecasts

Review of past week's data

Quarterly Labor Force Survey

Change from previous quarter (000s)

	2Q20	3Q20	4Q20	
Total employment	-2235	543	—	333
Unemployment rate (%)	23.3	30.8	—	32.5

Source: StatsSA, National Treasury, J.P. Morgan forecasts

SSA

Data releases and forecasts

Week of March 1 – 5

Kenya	Markit/Stanbic Bank PMI Index				
Wed Mar 3		Nov	Dec	Jan	Feb
	PMI	51.3	51.4	53.2	—
Nigeria	Markit/Stanbic IBTC Bank PMI Index				
Wed Mar 3		Nov	Dec	Jan	Feb
	PMI	50.9	51.8	50.7	—
Zambia	Markit/Stanbic Bank PMI Index				
Wed Mar 3		Nov	Dec	Jan	Feb
	PMI	49.3	49.0	47.7	—
Ghana	Markit/Stanbic Bank PMI Index				
Wed Mar 3		Nov	Dec	Jan	Feb
	PMI	52.5	50.3	51.2	—
M'bique	Markit/Stanbic Bank PMI Index				
Thu Mar 3		Nov	Dec	Jan	Feb
	PMI	49.4	49.5	47.5	—

MENA

- **GCC: Inflation pressures remain contained in the region**
- **Egypt: Industrial production still weak while employment rising sharply**
- **Pakistan: IMF program set to resume after the COVID-19-related suspension**

GCC: CPI prints remain weak across the region

In January, Saudi CPI inflation was just a bit lower than our forecast (5.7%oya vs. JPM: 5.8%oya) on a 0.2%m/m rise in the index. Food prices dropped 0.6% in the month, somewhat more than we expected. On the non-food front, house rents remain weak, declining once more in January (-0.1%m/m and -1.7%oya). The only significant upward price pressure came from transport (+2.0%m/m) due to an increase in fuel prices. Our forecast for 2021 remains for 3.6%/y headline CPI inflation, up from 3.5% in 2020, mostly due to the effect of the VAT increase in July 2020.

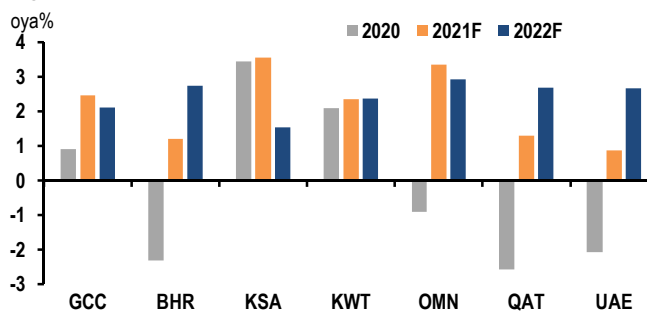
Looking at other GCC countries, the Oman CPI print was weaker than our forecast (-1.6%oya vs. JPM: -1.3%oya) with the price level unchanged from December. Alongside the effect that labor supply might have on Omani prices in months to come, the upcoming introduction of VAT in April will boost prices and as a consequence we expect 3.4% CPI inflation in 2021, following a 0.9% drop in 2019.

In Kuwait, CPI inflation was stable at 2.9%oya in January versus our expectation of a slowing to 2.7%oya. The slightly higher print does not change our for full-year 2021 CPI inflation at 2.3%/y, up from 2.1% a year ago.

Qatar also released January CPI data and in this case the surprise was to the upside, with prices declining moving 1.3%oya after a 3.4% fall in December. The 1.2%m/m monthly CPI increase, the strongest since August 2019, reflected large increases in several subsectors, notably transport, and furniture and household equipment. The higher-than-expected print resulted in us raising our forecast for 2021 to 1.3%/y from -2.6% in 2020.

Looking at the inflation outlook for the next couple of years (Figure 1), the large contraction in the expat population and the shift from employing expats to locals should put some pressure on wages as well as on availability of labor if the economy is able to pick up fast after the COVID-19 shock. As a consequence, we expect some inflationary pressure on core prices, as well as a more difficult transition toward a diversified economy with a potential drag on GDP growth.

Figure 1: GCC headline CPI



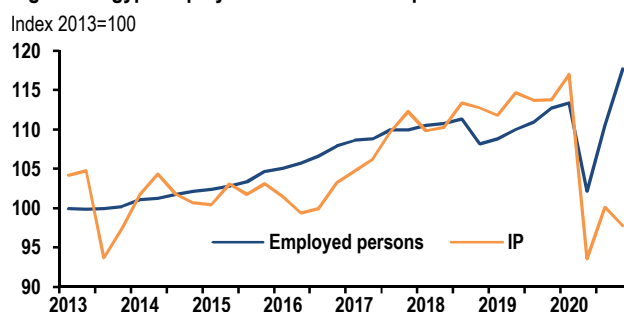
Source: Local authorities, J.P. Morgan - JPM forecast for 2021 and 2022

Egypt: High-frequency activity data remain weak despite strong labor market figures

High-frequency data provide mixed messages on the state of the Egyptian economy. Industrial production has struggled to recover with the index falling almost 3%m/m in December to be down 14.1%oya and. On the other hand, trade activity surged with exports picking up extremely fast in the last month of 2020. Exports grew 6.8%oya December and imports were up by 0.1%oya, after a sharp pickup in November. The trade deficit remained unchanged in December at US\$3.3bn, with the 2020 full-year deficit at US\$33.2bn, up from US\$46.9bn in 2019, demonstrating once more how the country was able to adjust in response to the COVID-19 shock. Suez Canal receipts were just slightly lower than in January 2020 (-0.58%oya). With receipts plunging -13.4%oya in June, as a result of the COVID-19 shock, full-year 2020 receipts declined by 3.4%, a deeper contraction than in 2015.

Despite contraction in industrial production, Egypt's labor market data were constructive with the unemployment rate down marginally to 7.2% in 4Q20, from 7.3% in 3Q and a 9.6% peak in 2Q20 (Figure 2). Employment growth continued, reaching 4.4%oya, after contracting by 0.3% in 3Q and 7.2% in 2Q.

Figure 2: Egypt employment and industrial production



Source: Local authorities, J.P. Morgan

Pakistan: After almost a year in limbo, the IMF program is set to resume

The Pakistani authorities and the IMF agreed to resume the US\$6bn EFF program that was suspended just before its second review due to the change in the economic outlook wrought by the pandemic. Discussions went on for several months with both parties committed to resuming the program despite not being able to reach an agreement. However, in recent months statements from officials as well as important concessions from Pakistani authorities (such as the increase in utility prices) signaled that the resumption of the EFF program was getting closer.

Before the program was suspended only one review was conducted with a total of just US\$1.4bn disbursed. A large amount remains to be disbursed under the EFF program with a US\$500mn disbursement schedule at the first review following the resumption. During the intervening period, the IMF continued its support with Pakistan receiving US\$1.4bn through the RFI program in April 2020. Moreover, the country received support from several other multilateral organizations and participated to the DSSI program, which suspended repayments to G-20 countries.

On the external side, due to resilient remittances inflows, a sharp trade adjustment, and multilateral support, Pakistan's current account deficit shrank and its international reserves position improved. However we expect some deterioration and the IMF program would help to reduce pressure on the external accounts. A difficult-to-predict and very resilient inflow of remittances together with low oil prices and a large import left the current account deficit at a low 1.1% of GDP in FY20. The modest annual deficit, and the surplus reported in the first five months of the new financial year started in June, together with multilateral and bilateral support helped to rebuild international reserves. However, pressure on the current account resumed in December and continued in January with the balance slipping into deficit. Higher imports on the back of economic recovery and a slowdown in remittances inflows due to the fading of some one-off COVID-19-related supports signal a widening deficit. We forecast the current account deficit to increase to 1.7% of GDP in FY21 and 2.9% in FY22. We believe that the inflow from the IMF program would be extremely beneficial to keep currency pressures at bay and to allow further rebuilding of international reserves.

Data releases and forecasts

Weeks of March 1 – 12

Egypt:

Wed Mar 3 9:00am	PMI Index				
	PMI, Composite	Nov	Dec	Jan	Feb
		50.9	48.2	48.7	—
Wed Mar 10 9:00am	Consumer prices %oya				
	%oya	Nov	Dec	Jan	Feb
		5.7	5.4	4.3	<u>5.2</u>
	%m/m nsa	0.8	-0.4	-0.4	—
	Core	4.0	3.8	3.6	—
	Food	3.7	2.8	-0.5	—
	Housing	4.3	4.4	4.3	—
	Transport	4.1	4.1	3.6	—

Saudi Arabia:

Wed Mar 3 9:00am	PMI Index				
	PMI, Composite	Nov	Dec	Jan	Feb
		54.7	57.0	57.1	—

Review of past week's data

Egypt:

External trade

USD bn				
	Oct	Nov	Dec	
Trade balance	-2.9	-3.3	—	-3.3
Ytd	-73.6	-76.8	—	-80
Ytd a year ago	-40.5	-43.5	-46.9	
Exports %oya	2.2	2.2	—	2.8
Imports %oya	5.1	5.5	—	6.0

Saudi Arabia:

Consumer prices

%oya				
	Nov	Dec	Jan	
%oya	5.8	5.4	<u>5.8</u>	5.7
%m/m nsa	-0.1	-0.2	—	0.2
Food	13.0	12.8	—	12.3
Housing	-0.8	-1.5	—	-0.9
Transport	8.0	6.9	—	9.5

SAMA net foreign assets

SAR bn				
	Nov	Dec	Jan	
	1696	1684	—	1671

Source: CBE, MoPE, GASTAT, SAMA, Markit, J.P. Morgan forecasts

Australia and New Zealand

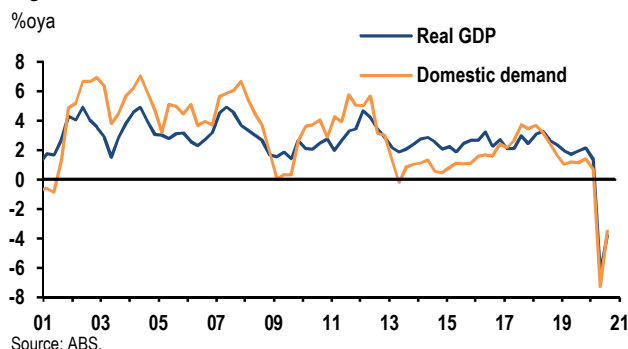
- We expect the RBA to stick to script in the coming week's March meeting
- Australia's 4Q real GDP print forecast to increase 1.6%/q/q, led by strong household consumption
- We anticipate modest gains in the retail sales and trade data for January
- RBNZ retains optionality but left policy settings unchanged at the February meeting

Despite the volatility in fixed income markets and the dislocation of short-end rates from current guidance, we expect next week's RBA meeting to be uneventful. The RBA's reaction function regarding yield curve control (YCC) is pretty clear, so there isn't much scope to get more specific at the coming meeting, particularly given the RBA has already recommenced purchases in the past week. There is indeed uncertainty as to whether YCC will be rolled in July, but the target still exists today, and the RBA's language reflects the degree of the board's "certainty" about the outlook for the cash rate. Relatedly, we expect the policy statement to repeat February's guidance verbatim, noting conditions for rate hikes are unlikely "to be met until 2024 at the earliest."

Strong end to 2020...

The Australian economy is forecast to have increased 1.6%/q/q in the final quarter of 2020 with activity continuing to rebound following the sharp contraction earlier in the year (Figure 1). Consumption is expected to rebound 3.5%/q/q, buoyed by the ongoing recovery in services spending as the economy gradually reopens. The reopening of the Victorian economy in late 3Q20 will also boost the headline GDP print, with the retail data indicating spending activity in that state outpaced the rest of Australia in 4Q.

Figure 1: Australian real GDP and domestic demand



Last week's construction and capex data were mixed, though in net terms were broadly offsetting and didn't materially alter

our expectation for near-term GDP. The forward-looking component of the capex survey suggests investment intentions are marginally weaker than we had anticipated, but we expect these to be lifted over time as uncertainty subsides and vaccines are rolled out. Net trade should be a headwind as the reported spike in real imports outpaces the only modest growth in export volumes. Early next week the ABS releases more data on government spending, net trade, and company profits. We will update our tracking framework following the release of these data points.

...and first look at 2021 activity data

Next week also sees the release of the activity data for January. The preliminary retail sales print suggested sales activity ticked higher at the start of the year (0.6%/m/m), with the three-day lockdown in Queensland weighing on retail activity in that state. Food retailing was strong, though was offset, to an extent, by weaker outcomes in clothing, footwear/personal accessory retailing, household goods retailing, and department stores. Since its implementation earlier in the year the preliminary data have served as a reliable proxy for the final outcome, so we anticipate a relatively modest increase in this week's print.

The preliminary trade data have proven less reliable than their retail counterpart, largely due to their highly revision-prone nature. With that in mind, we expect Australia's trade surplus to widen to A\$8 billion in this week's print for January. The data are particularly difficult to decipher early in the year given the shifting timing of Lunar New Year distorts seasonal demand patterns, but the higher-frequency port data alongside the strength in key commodity prices are consistent with our forecasts for an improvement in the trade surplus.

Lastly, building approvals were very strong in the final quarter of 2020 and suggest that residential activity is responding to low rates following subdued activity earlier in the year. The December print was particularly strong (10.9%/m/m), so a degree of payback is likely in January's update. That said, low rates and rising housing prices are generally supportive for residential investment activity and we forecast continued strength in the building approvals data through 2021.

RBNZ retains optionality

The RBNZ left the OCR unchanged at 0.25% this past week and delivered a mixed statement that left the outlook open-ended, and so somewhat in the eye of the beholder. On the guidance front, the bank went with words rather than numbers: instead of issuing an on-hold OCR track as expected it opted to keep all possibilities open, citing a "highly uncertain" outlook. The labor market has been "more resilient than anticipated," though the committee still sees its goals as distant.

Getting there will take “a prolonged period,” and require “considerable time and patience.”

The MPS document includes the “unconstrained OCR” modeling that was prominent last year. The path is higher than before, but still negative. As noted above, operational constraints to a negative OCR are apparently dealt with, which would suggest the unconstrained path should equal the actual path. QE accounts for the gap, but as that is now running into its own constraints, the appropriate policy rate still seems to be biased to lower than current levels. We remain confident the RBNZ is unlikely to hike, and the bias is skewed toward cuts later in the year once LVR restrictions gain traction on housing, though we are tactically short AUD/NZD given the RBNZ’s inability to do anything particularly dovish in actions or guidance right now.

Australia

Data releases and forecasts

Week of March 1 – 5

Mon	Company profits				
Mar 1		Mar	Jun	Sep	Dec
11:30am	%q/q	0.6	15.8	3.2	<u>1.0</u>
Mon	Inventories				
Mar 1		Mar	Jun	Sep	Dec
11:30am	%q/q	0.5	-2.9	-0.5	<u>-0.8</u>
Tue	Current account balance				
Mar 2		Mar	Jun	Sep	Dec
11:30am	A\$bn	9.0	16.3	10.0	<u>10.0</u>
Tue	Net exports of GDP				
Mar 2		Mar	Jun	Sep	Dec
11:30am	%-pts	0.3	1.0	-2.0	<u>-0.8</u>
Tue	Building approvals				
Mar 2		Oct	Nov	Dec	Jan
11:30am	%m/m	2.6	3.4	10.9	<u>-1.0</u>
Wed	Real GDP				
Mar 3		Mar	Jun	Sep	Dec
11:30am	%q/q	-0.7	-7.0	3.3	<u>1.6</u>
Thu	Trade balance				
Mar 4		Oct	Nov	Dec	Jan
11:30am	A\$bn	8.1	5.0	6.8	<u>8.0</u>

Thu	Retail sales				
Mar 4		Oct	Nov	Dec	Jan
11:30am	%m/m	1.4	7.0	-4.1	<u>0.6</u>

Review of prior week’s data

Private wages ex overtime

	Jun	Sep	Dec
%q/q	0.2	0.1	0.6

Construction work done

	Jun	Sep	Dec
%q/q	-2.0	-1.8	-0.9

Private capital expenditure

	Jun	Sep	Dec
%q/q	-5.9	-3.0	3.0

New Zealand

Data releases and forecasts

Week of March 1 – 5

Mon	Terms of trade				
Mar 1		Mar	Jun	Sep	Dec
11:30am	%q/q	2.5	2.4	-4.7	-

Review of prior week’s data

Retail volumes

	Jun	Sep	Dec
%q/q	-14.9	27.8	-2.7

Source: ABS, Stats NZ, J.P. Morgan forecasts

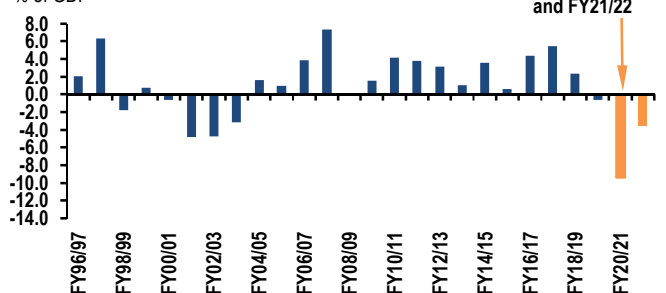
Greater China

- **Hong Kong: FY21/22 budget points to continuous, targeted fiscal support**
- **January CPI inflation beat expectation, rising 1.9%oya**
- **January trade activity saw strong year-on-year growth on low-base and LNY effects**
- **Revising up 2021 growth forecast**
- **Taiwan: 4Q20 GDP growth revised up to 5.09%oya**
- **January export orders showed continuous, broad-based demand strength**
- **Steady growth in January IP with inventory shipment ratio down to six-year low**
- **Revising up 2021 growth forecast on strong growth**

Amid the economic recession under the prolonged pandemic, Hong Kong's FY21/22 budget aims to stabilize the economy and relieve the social burden with continuous and targeted supportive measures, registering another fiscal deficit at HK\$101.6 billion, about 3.6% of GDP (Figure 1). Given the counter-cyclical measures amounting to over HK\$120 billion, followed by several rounds of anti-epidemic funds and relief measures to revive the economy, the government also revised the estimates for FY20/21, with the fiscal balance registering a record-high deficit at HK\$257.6 billion, about 9.4% of GDP. The government is also looking for a continued fiscal deficit until FY25/26.

Figure 1: Hong Kong fiscal balance

% of GDP



Source: HK Government

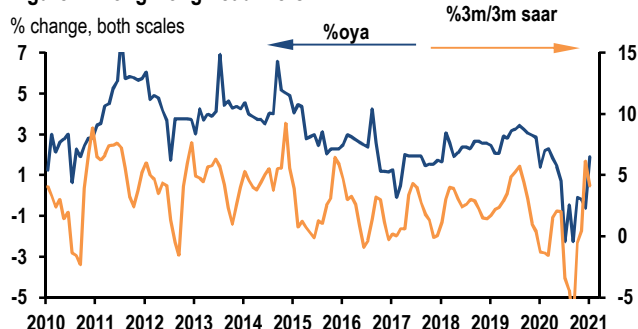
With the significantly widened fiscal deficit through FY2020/21, the fiscal space has constrained the government's capacity, but the relief measures announced this week remain supportive, targeting the hardship encountered by the private sector, with government-backed loans extended, low-interest loans for the unemployed, and HK\$5,000 consumption coupons. Compared to the elevated fiscal deficit for FY20/21, the announced FY21/22 fiscal budget represents a fiscal drag of

5.9% of GDP, though we can still expect other anti-epidemic packages to come, depending on the COVID-19 situation and vaccination progress.

January CPI inflation beat expectation, rising 1.9%oya

January headline CPI surprised the market to the upside, roaring 1.9%oya or 1.1%/m/m, sa (Figure 2). The substantial increase in the year-on-year headline inflation was led by a low base effect resulting from the government's housing cost- and electricity-related subsidies last January. After netting out the effects of the government's one-off relief measures, underlying CPI inflation printed at -0.5%oya in January.

Figure 2: Hong Kong headline CPI



Source: HK C&SD

We expect food prices to increase sequentially in the near term with relatively supportive consumption demand during the LNY holiday and recent loosening in social distancing measures. After the sharp rise in January electricity prices, we expect non-housing services CPI to soften in the next few months. Overall, we expect headline CPI to rise 2.1%oya in 2021 (vs 0.3%oya in 2020), while core CPI trends up to 1.4%oya in 2021 (vs. -0.2%oya in 2020).

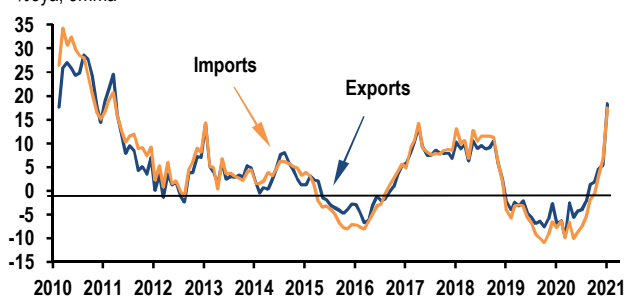
January trade activity saw strong year-on-year growth on low base and LNY effects

January trade activity grew in the high double-digits, mainly on low base and LNY effects. Export growth spiked to 44.0%oya in January from 11.7% in December and import growth also accelerated to 37.7%oya in January from 14.1% in December (Figure 3). Overall, January posted a HK\$25.2 billion visible trade deficit.

We expect a continued recovery in the trade sector, though this view needs further data from February to correct for seasonal effects. With the solid global economic growth recovery led by the US, which growing 6.4%oya in 2021, and continued recovery in the Mainland, we expect Hong Kong trade to recover further this year, given its high proportion of re-exports, which would also feed the labor market recovery.

Figure 3: Hong Kong merchandise trade

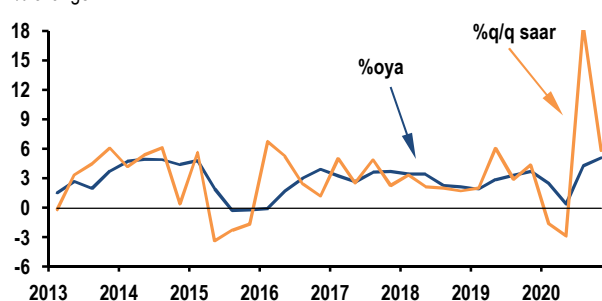
%oya, 3mma



Source: HK C&SD, J.P. Morgan

Figure 4: Taiwan real GDP growth

% change



Source: DGBAS, J.P. Morgan

Revising up 2021 growth forecasts

In line with the advance reading, the final prints of 4Q20 GDP contracted 3.0%oya, and Hong Kong's GDP contracted 6.1%/y in full-year 2020.

Looking ahead, on the consumption front, coupons totaling HK\$36 billion together with loosened social distancing measures will benefit private consumption. On the tourism front, the government announced it will allocate more than HK\$900 million to related sectors, and resume travel bubble arrangements. On the external front, we expect the US to outperform China's V-shaped recovery.

Overall, we raise our sequential growth forecast in 1Q21 to 3.9%/q saar, followed by the trajectory of – 2Q: 8.0%; 3Q: 7.4%; 4Q: 3.8%. Our forecast for 2021 full-year GDP growth now stands at 5.2%oya (previously 4.9%oya), while downside risks remain.

Taiwan: 4Q20 GDP growth revised up to 5.09%oya

Taiwan's 4Q20 real GDP has been revised up to solid 5.09%oya growth (vs. +4.94%oya in the advance 4Q GDP report, Figure 4), following upwardly-revised 3Q growth at 4.26%oya (previously: 3.92%oya). Seasonally-adjusted, GDP expanded 5.8%/q, saar in 4Q, following upwardly-revised 18.5%/q, saar growth in 3Q. For full-year 2020, Taiwan's real GDP grew 3.11%/y.

Details in the 4Q20 GDP report highlight further broad-based recovery in exports and private consumption, along with a notable rebound in fixed investment. Overall, Taiwan's economy showed surprising strength in 2020, when the global economy was badly hit by the unexpected COVID-19 shock. Successful containment of the virus infection at an early stage, surging WFH-related tech demand, and ongoing re-shoring of production lines back to Taiwan have contributed to the economy's strong performance.

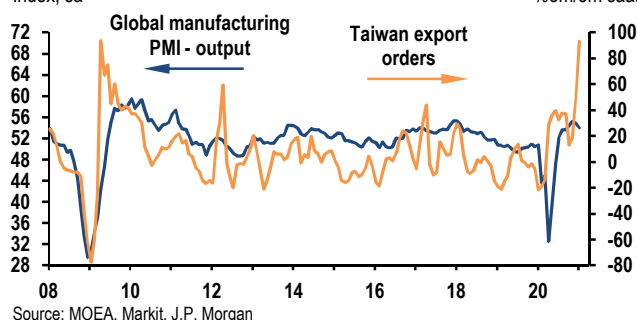
January export orders showed continuous, broad-based demand strength

Taiwan's January export orders beat expectations again, adding to the surprising strength in December and November, rising 49.3%oya with a fall of 4.0%/m, sa (Figure 5). By major product category, tech sector demand held up well in January following recent sharp acceleration, edging down 0.7%/m, sa, while non-tech orders grew a solid 2.1%/m, sa in January.

Figure 5: Global manufacturing PMI and Taiwan export orders

Index, sa

%3m/3m saar



Source: MOEA, Markit, J.P. Morgan

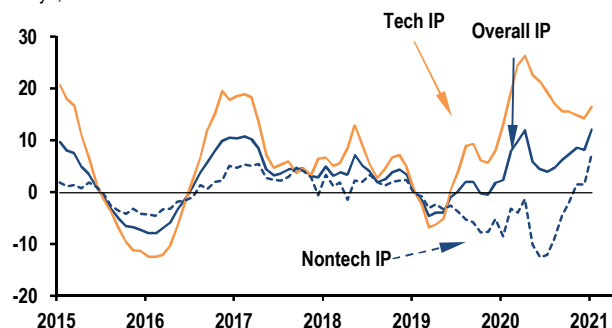
In the near term, early signals suggest Taiwan's export orders momentum will likely remain solid in February despite the lunar New Year holiday. Overall, the constructive global demand outlook, along with sustained, structural tech demand strength, should support further solid export growth for Taiwan, especially from 2Q21 onwards.

Steady growth in January IP with inventory shipment ratio down to six-year low

January's IP report showed steady 18.8%oya growth following the notable 10.29%oya uptick in December. Tech-related IP rose 5.5%/m, sa, while non-tech IP fell 2.1%/m, sa (Figure 6). Domestic consumption seems to have stabilized after the deceleration in December, as retail sales rose 0.8%/m, sa in January.

Figure 6: Taiwan IP growth breakdown

%oya, 3mma



Source: J.P. Morgan

The inventory-to-shipment ratio has fallen to a six-year low, after the notable adjustment through December. Lean inventory conditions, along with a solid external demand trend, suggest the inventory cycle would be another supportive factor for manufacturing activity in the near term. With the constructive external demand outlook, Taiwan's tech sector appears to be pushing for further significant capex expansion in the coming quarters.

Revising up 2021 growth forecast on strong growth strength

Looking ahead, we expect Taiwan's economic growth to stabilize in 1Q21 (at around 4.0%/q, saar), as a modest increase in local virus cases likely exerted a moderate drag on domestic spending around the Lunar New Year holiday season.

The constructive global demand outlook, along with sustained, structural tech demand strength, should support further solid export growth for Taiwan, especially from 2Q21 onwards. Overall, we expect Taiwan's growth momentum to pick up notably (to average 6.1%/q, saar in 2Q-3Q) with the global rollout of vaccinations and the generous fiscal support in the US. Overall, we expect Taiwan's full-year 2021 GDP to grow at a strong 6.2%/y.

China:**Data releases and forecasts****Week of March 1 - 5**

Sun	Purchasing managers index				
Feb 28	Index				
9:00am		Nov	Dec	Jan	Feb
	Overall (NBS)	52.1	51.9	51.3	<u>51.2</u>
	Output	54.7	54.2	53.5	—

Mon	Purchasing managers index				
Mar 1	Index				
9:00am		Nov	Dec	Jan	Feb
	Overall (Markit)	54.9	53.0	51.5	<u>51.5</u>
	Output	57.1	55.4	52.5	—

Review of past week's data

No data released.

Hong Kong SAR:**Data releases and forecasts****Week of March 1 - 5**

Wed	Retail sales volume				
Mar 3	% change				
4:30pm		Oct	Nov	Dec	Jan
	%oya	-9.2	-4.7	-14.0	<u>-11.0</u>
	%m/m sa	-0.4	2.7	-2.6	<u>0.8</u>

Review of past week's data**Consumer prices (22 Feb)**

% change	Nov	Dec	Jan	
%oya	-0.2	-0.6	<u>1.2</u>	1.9
%m/m sa	0.0	-0.3	<u>0.1</u>	1.4

Real GDP (24 Feb)

% change	20Q2	20Q3	20Q4	
%oya	-9.0	-3.6	<u>-3.0</u>	
%q/q saar	-0.3	11.4	<u>0.8</u>	0.7

Merchandise trade (25 Feb)

HK\$ bn	Nov	Dec	Jan	
Balance	-25.6	-45.7	<u>-8.8</u>	-25.2
Exports	379.6	392.2	<u>360.4</u>	388.0
%oya	5.6	11.7	<u>33.8</u>	44.0
Imports	405.2	438.0	<u>369.2</u>	413.2
%oya	5.1	14.1	<u>23.1</u>	37.7

Taiwan:**Data releases and forecasts****Week of March 1 - 5**

Tue	Markit manufacturing PMI				
Mar 2	Index, sa				
8:30am		Nov	Dec	Jan	Feb
	Overall	56.9	59.4	60.2	<u>59.8</u>
	Output	57.9	59.9	58.8	—

Review of past week's data**Real GDP (20 Feb)**

% change	20Q2	20Q3	20Q4	
%oya	0.3	4.3	<u>4.9</u>	5.1
%q/q saar	-2.9	18.5	<u>7.8</u>	5.8

Export orders (24 Feb)

% change	Nov	Dec	Jan	
%oya	29.7	38.3	<u>46.2</u>	49.3
%m/m, sa	12.1	9.8	<u>-5.4</u>	-4.0

Labor market survey (25 Feb)

%	Nov	Dec	Jan	
Unemployment rate, sa	3.77	3.76	<u>3.74</u>	3.75
Unemployment rate,	3.75	3.68	<u>3.65</u>	3.66

Industrial production (25 Feb)

% change	Nov	Dec	Jan	
%oya	7.7	10.3	<u>19.2</u>	18.8
%m/m sa	0.8	3.4	<u>0.4</u>	0.3

Source: NBS, China Customs, Hong Kong Census and Statistics Department, Taiwan Ministry of Economic Affairs, DGBAS, MoF, J.P. Morgan forecasts

Korea

- We now expect the BoK's next move to be a hike next year
- 20-day reports hints at continued exports growth in February
- Households increased leverage amid a recovery in consumer sentiment

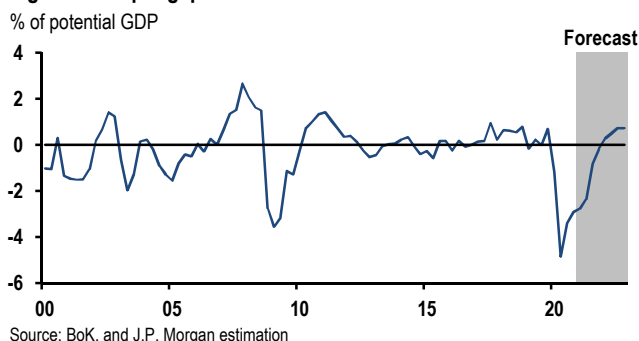
As broadly expected, the Bank of Korea maintained its base policy rate and forward guidance at its February meeting. The post-MPC communication confirmed that the BoK is not ready for an exit plan yet, and it maintained its 2021 growth outlook. However, we now see greater upside risk to its outlook, changing our call on the next move to a hike in 1Q22 and another in 3Q22.

We changed our call on BoK's next move

The BoK's policy guidance was unchanged at February's uneventful meeting, implying that the BoK is not ready for an exit plan yet as we observed in January's meeting. While the BoK's outlook on external demand and facility investment is more encouraging, the private consumption recovery is weaker than its previous forecast with a larger drag on employment from the lingering COVID-19 impact. To be sure, against our expectation, the BoK kept its 2021 full-year GDP growth forecast at 3.0%/y, although it upgraded its global growth assumption and real exports forecast, offset by a downgrade in private consumption growth. That said, in our view, its risk bias on the growth outlook likely shifted to the upside. While the BoK did not raise the growth outlook at this meeting due to a lack of confidence in the speed of the private consumption recovery, it should see an improving risk profile from more upbeat external demand conditions and additional fiscal stimulus in the pipeline (the government intends to submit a 1.0% of GDP supplementary budget in early March, which the BoK's current forecast does not reflect).

In our previous assessments of the BoK's stance, we had highlighted the risk of a hawkish signal this year implying that normalization might start next year. After the January MPC meeting, we upgraded our 2021 GDP growth forecast from 3.5%/y to 4.0%, based on a higher global growth forecast and a stronger-than-expected 4Q20 GDP outcome; thus, we see a stronger case for a hawkish risk bias at the BoK. We now expect the output gap to close in early 2022 after narrowing rapidly in 2H21 (Figure 1), and this projection implies a firming of core price gains to a mid-to-upper 1% pace. Financial imbalance issues from elevated household leverage have always been incorporated in the MPC's outlook, and the narrowing of the output gap and recovery in inflation should ultimately imply that the financial imbalances will have more weight in the MPC's reaction function.

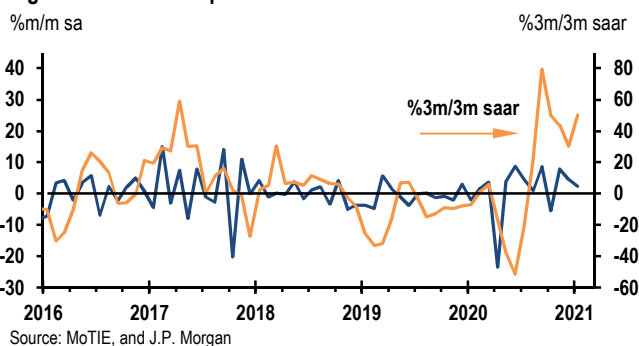
Figure 1: Output gap



The timing and speed of policy rate normalization is highly uncertain, given the lack of a clear signal from the BoK. Tentatively, we expect that hawkish dissent vote(s) will emerge in 4Q21, about the time when most of the population should be vaccinated (according to the government's target), %oia real GDP growth could reach about 5% (in our projections), and we expect the US Fed to announce tapering of asset purchases. We expect the BoK to actually hike rates in 1Q22 and 3Q22 by 25bp each. That said, we will reassess the timing and pace of rate normalization as the BoK provides further data and signals.

Strong exports growth should continue in February

Figure 2: Customs exports

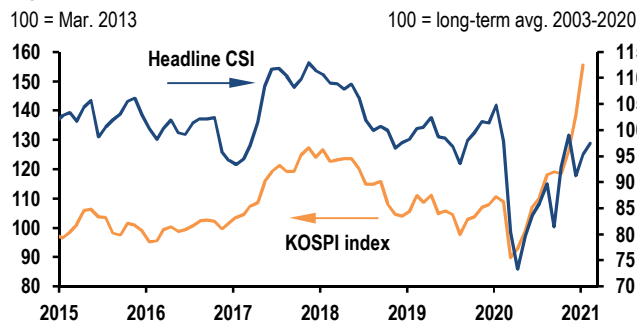


Customs exports during the first 20 days of February rose 16.7%oia. If we adjust for trading day differences, then we estimate full-month exports will rise 12.0%oia in February, which is lower than the 20.7% estimate from the 10-day data, reflecting payback from pre-holiday front-loading. The 20-day data imply a 3.3%/m, sa gain (vs. 8.7% implied by 10-day data). Looking through the Lunar New Year holiday noise, exports are likely to rise robustly further in February on top of the gains in 4Q20 and January, which would imply about a 50% annualized three-month trend gain following 30.4%3m/3m, saar growth in December (Figure 2).

Households are increasing leverage amid sentiment recovery

The consumer sentiment index rose further in February, continuing its recovery from last April's trough due to the COVID-19 shock (Figure 3). The most recent COVID-19 daily case count lingers around the previous peak in September, yet the drag on consumer sentiment has been relatively muted compared with previous resurgences as consumers have adapted to the outbreaks. Meanwhile, household credit grew a stronger-than-expected 8.8%q/q, saar in 4Q20, in part as rising asset prices fueled greater loan demand to finance leveraged investments.

Figure 3: Headline CSI and KOSPI



Source: BoK, KRX and J.P. Morgan

Data releases and forecasts

Week of March 1 – 5

Mon Mar 1 9:00am	Customs trade US\$ bn, nsa				
		Nov	Dec	Jan	Feb
	Trade balance	5.8	6.7	3.8	<u>1.8</u>
	Exports	45.8	51.3	48.0	<u>45.8</u>
	Imports	39.9	44.6	44.3	<u>44.0</u>

Tue Mar 2 8:00am	Industrial production % change				
		Oct	Nov	Dec	Jan
	%oya	-2.1	0.5	3.4	<u>12.0</u>
	%m/m, sa	-1.2	0.3	3.7	<u>2.0</u>

High-frequency indicators suggested that automobile production should rebound strongly in January, and robust underlying trend growth in exports should continue to support overall IP growth.

Tue Mar 2 8:00am	Producer shipments and inventories %oya				
		Oct	Nov	Dec	Jan
	Shipments	-3.0	1.2	2.3	<u>13.8</u>
	Inventories	-0.1	-1.1	1.4	<u>-1.5</u>

Tue Mar 2 8:00am	Composite leading indicator 2015=100, sa				
		Oct	Nov	Dec	Jan
	Index	122.8	123.9	124.8	<u>125.6</u>

Tue Mar 2 8:00am	Service activity % change				
		Oct	Nov	Dec	Jan
	%oya	-2.5	-1.4	-2.2	<u>-3.4</u>

Tue Mar 2 8:00am	Consumption goods sales % change				
		Oct	Nov	Dec	Jan
	%oya	-0.2	-1.5	-2.0	<u>0.9</u>
	%m/m, sa	-1.0	-0.9	0.2	<u>2.0</u>

Tue Mar 2 9:30am	Purchasing Managers Index Index, sa				
		Nov	Dec	Jan	Feb
	PMI - Manufacturing	52.9	52.9	53.2	<u>53.5</u>

Thu Mar 4 8:00am	Consumer prices % change				
		Nov	Dec	Jan	Feb
	%oya	0.6	0.5	0.6	<u>1.3</u>
	%m/m, nsa	-0.1	0.2	0.8	<u>0.7</u>

Thu Mar 4 8:00am	Real GDP 2nd estimate % change				
		1Q20	2Q20	3Q20	4Q20
	%q/q, sa	-1.3	-3.2	2.1	<u>1.1</u>
	%q/q, saar	-5.0	-12.0	8.8	<u>4.4</u>
	%oya	1.4	-2.7	-1.1	<u>-1.4</u>

Review of past week's data

Consumer survey (Feb 23)

100=neutral reading, nsa				
	Dec	Jan	Feb	
Index	91.2	95.4	<u>96.0</u>	97.4

Household credit (Feb 23)

% change				
	2Q20	3Q20	4Q20	
%oya	5.2	7.0	<u>7.4</u>	7.9

FKI business survey (Feb 24)

Index, sa				
	Dec	Jan	Feb	
One-month outlook	<u>90.2</u>	90.5	<u>104.4</u>	102.0
Current conditions	<u>90.9</u>	91.1	<u>100.4</u>	96.8
			<u>101.0</u>	106.4

Source: Customs office, NSO, Markit, BoK, FKI, and J.P. Morgan forecasts

ASEAN

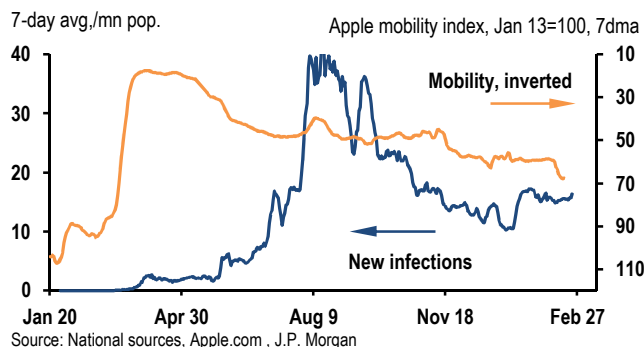
- **Mobility restrictions in the Philippines likely to be extended in the absence of a wide-scale vaccination rollout**
- **The BSP will likely stay on hold through 2021 despite inflation set to remain at or above the upper-end target**
- **Overall BoP printed a record US\$16bn surplus in 2020; we expect another, much smaller, surplus in 2021**

The narrative for the Philippines of a fragile economic recovery and a trade deficit that will likely widen in the second half of the year remains broadly intact. The long-standing mobility restrictions across the Philippines, and in particular in the Metro Manila area, are likely to be extended yet again until the mass vaccination drive is under way. With suppressed domestic demand and a capex cycle upturn that we think will only get underway in 2H21, the economic recovery will likely be lackluster. Meanwhile headline inflation is set to remain elevated at or above the BSP target in coming months due to supply-side increases in food and transport prices. In this context, we think the BSP will remain on hold through 2021 keeping the policy setting, particularly fiscal policy, accommodative.

Movement control orders to remain in place

The long-standing mobility restrictions across the Philippines, with Metro Manila and surrounding regions under community quarantines since March last year, are likely to be extended yet again beyond the end of February. This is because [authorities have rejected calls to ease mobility restrictions](#) without a wide-scale vaccine roll-out and shipment dates of vaccines are yet to be finalized. While some lockdown measures have been relaxed, mobility indicators have remained stubborn around 50%-70% of pre-COVID-19 levels for nearly nine months (Figure 1). With slim prospects of tourism or domestic demand picking up in the near term, we maintain our view that the economic recovery will be fragile and skewed to the second half of this year in line with the capex cycle upturn.

Figure 1: Philippines daily new infection and mobility index



BSP to stay on hold through 2021 despite target-breaching inflation

Headline inflation has now surprised to the upside for three consecutive months and most recently [breached](#) the upper end of the BSP's $3.0\% \pm 1.0\%$ inflation target (Figure 2). A surge in food prices and transport costs continues to drive the high inflation prints (Figure 3). The rise in food prices remains attributable to supply-side pressures from both the typhoons and African swine fever on meat products in particular. Looking ahead, the [recent price caps](#) for 60 days on such meat products should ease the pressure. Meanwhile, transport costs also inched higher for the third month in a row in line with rising oil prices. We think there is scope for transport costs to remain elevated in line with our commodity strategists' forecast of Brent oil prices averaging US\$61 throughout 2021.

Figure 2: Headline inflation

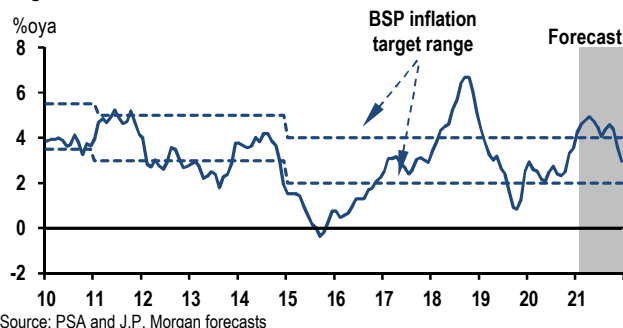
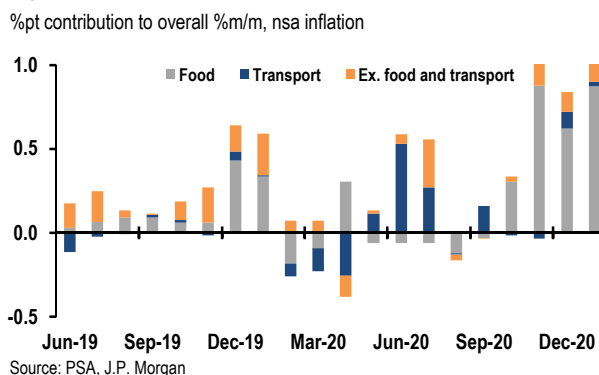


Figure 3: Contribution to inflation



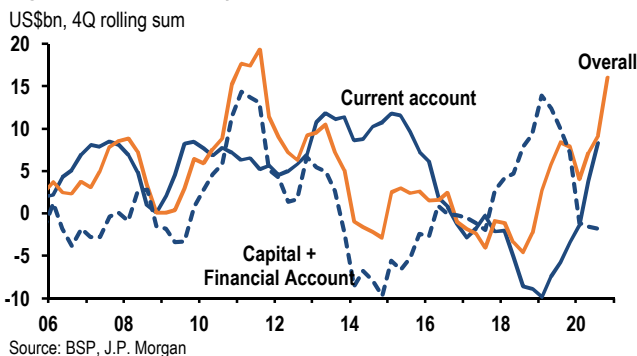
We expect the BSP to remain on hold through 2021, looking past the transitory supply-side inflationary pressures, considering the fragile economic recovery. We expect headline inflation to remain elevated at or above the BSP target in coming months due to supply-side increases in food and transport prices. Despite the elevated inflation prints, we expect the BSP will remain on hold through 2021 keeping the policy

setting accommodative and focusing on the lackluster economic recovery considering that the supply-side related increases especially in food prices should be temporary.

Overall BoP to remain in a surplus this year, following 2020's stellar performance

The Philippines posted its first monthly overall balance of payments (BoP) deficit in a year at -US\$752mn in January. This followed the US\$4.2bn BoP surplus in December, which was the largest on record since 1999, due to a combination of US\$2.75bn Eurobond proceeds, a lower-than-anticipated trade deficit, and sustained net inflows from overseas worker remittances and inward FDI. The December print brought the 2020 full-year BoP surplus to US\$16bn (4.3% of GDP), which was the largest full-year BoP surplus on record since 1999 (Figure 4). Looking ahead, considering the slow economic revival, we think a substantial widening of the trade deficit will likely only materialize further down the line in 2H21. So the dichotomy of strong exports and suppressed imports will likely continue and keep the current account in a surplus in 2021, although not as large as last year's. We expect this to continue supporting overall BoP dynamics although pencil in a much smaller surplus (US\$2bn in 2021) in line with a normalization of the economy.

Figure 4: Balance of payments



ASEAN

Indonesia

Data releases and forecasts

Week of March 1 – 5

Mon	Consumer prices				
Mar 1	% change				
11:00am		Nov	Dec	Jan	Feb
	Total, %oya	1.6	1.7	1.6	<u>1.6</u>
	%m/m, sa	0.2	0.2	0.2	<u>0.2</u>

Review of past week's data

No data releases.

Malaysia

Data releases and forecasts

Week of March 1 – 5

Thu	BNM monetary policy meeting				
Feb 4	% pa				
		Dec	Jan	Feb	Mar
	Overnight policy rate	1.75	1.75	1.75	<u>1.75</u>

Review of past week's data

Consumer prices (Feb 23)

% change	Nov	Dec	Jan	
All items, %oya	-1.7	-1.4	<u>-1.3</u>	-0.2
%m/m, sa	-0.2	0.5	<u>0.2</u>	1.2

Malaysia consumer prices increased 1.2%/m, sa, in January, leaving headline CPI at -0.2%oya (J.P. Morgan: -1.3%oya and consensus: -1.4%oya). In sequential terms, headline CPI increased to 2.6%3m/3m, saar, after slowing in the previous three months. Accounting for the upside print in January, we now think that headline inflation will average higher in 2021 at 2.5%oya, from -1.2%oya in 2020. Meanwhile, core prices, which exclude the most volatile fresh food items and administered prices of goods & services, rose marginally by 0.1%/m, sa. Overall core inflationary pressures remain muted with monthly sequential prints averaging less than 0.1%, and the over-year-ago figure remaining stable at 0.7%oya in January for the third consecutive month.

Merchandise trade (Feb 26)

US\$ bn, nsa	Nov	Dec	Jan	
Trade balance	4.1	5.1	<u>4.9</u>	4.1
Exports, %oya	5.7	13.3	<u>13.3</u>	7.7
Imports, %oya	-8.0	3.9	<u>5.1</u>	2.4

Malaysia's trade balance started the year at a US\$4.1 billion surplus, down from the US\$5.1 billion surplus in December. Following the sharp bounces in both imports and exports at the end of last year. Exports and imports both dipped in sequential terms in line with what we previously mentioned in terms of a slowdown in the first part of this year given the Movement Control Order (MCO) restrictions that are in place.

Philippines:

Data releases and forecasts

Week of March 1 – 5

Fri	Consumer prices				
Mar 5	% change				
9:00am		Nov	Dec	Jan	Feb
	Total, %oya	3.3	3.5	4.2	<u>4.6</u>
	%m/m, sa	1.0	0.8	0.9	<u>0.3</u>

Review of past week's data

No data releases.

Singapore:

Data releases and forecasts

Week of March 1 – 5

Tue	Purchasing managers index				
Mar 2	% change				
9:00pm		Nov	Dec	Jan	Feb
	PMI	50.4	50.5	50.7	<u>50.7</u>
	PMI—electronics	51.1	51.2	51.0	<u>51.0</u>

Review of past week's data

Consumer prices (Feb 23)

% change	Nov	Dec	Jan	
%oya	-0.1	0.0	<u>0.0</u>	0.2
%m/m, sa	-0.1	0.4	<u>0.0</u>	0.5

Given the turn in the economy, prospects for core inflation are likely to move up in sequential terms during 1Q21. Despite the cyclical revival, the damage to employment remains material. Employment could recover with a lag following a decline that has surpassed that of the 2008 crisis. As with output, the bulk of the employment decline has come from the non-manufacturing sectors, and given the anticipation of a multi-speed recovery across the various service sectors, we expect the employment recovery to be similarly variegated.

Industrial production (Feb 26)

% change	Nov	Dec	Jan	
%oya	19.4	16.2	<u>-1.8</u>	8.6
%m/m, sa	4.3	1.4	<u>-3.4</u>	4.6

Singapore's January industrial production rose 4.6%/m, sa to be up 8.6%oya (consensus: 4.4%oya). In sequential terms, overall industrial output contracted 8.2%/3m/3m, saar but was up 28.2%/3m/3m, saar excluding the volatile biomedical sector.

Thailand:

Data releases and forecasts

Week of March 1 – 5

Fri	Consumer prices				
Mar 5	% change				
10:30am		Nov	Dec	Jan	Feb
	Total, %oya	-0.4	-0.3	-0.3	<u>-0.1</u>
	%m/m, sa	0.2	0.5	0.1	<u>0.1</u>

Review of past week's data

Manufacturing production (Feb 25)

% change	Nov	Dec	Jan	
%oya	-0.6	-2.8	<u>-5.3</u>	-2.8
%m/m, sa	-1.2	1.7	<u>=</u>	-0.1

Private investment index (Feb 25)

% change	Nov	Dec	Jan	
%oya	0.9	6.2	<u>5.3</u>	1.3
%m/m, sa	2.2	6.2	<u>1.1</u>	-2.1

Private consumption index (Feb 25)

% change	Nov	Dec	Jan	
%oya	3.2	-1.2	<u>-2.1</u>	-7.2
%m/m, sa	1.1	-3.4	<u>1.2</u>	-3.7

Merchandise trade (Feb 25)

% change	Nov	Dec	Jan	
Trade balance	1.9	2.8	<u>2.0</u>	1.9
Exports, %oya	-3.1	4.6	<u>2.7</u>	-0.3
Imports, %oya	-3.3	-0.1	<u>-8.0</u>	-6.9

Thailand's January macroeconomic indicators suggest a mixed recovery, with manufacturing stabilizing from December levels even as consumption contracted amid a rise in COVID-19 cases, with the contraction most apparent in services and non-durables consumption. Private investment has remained stable despite the slowing in consumption.

We continue to watch the evolution of the balance of payments, especially the current account balance given weakness in services exports and resumption of capital spending. The risk is that the lagged recovery in tourism inflows could, amid a capex recovery and rising oil prices, lead to a further decline of the current account balance into the red. Indeed, the January current account balance dipped into a US\$0.7 billion deficit and the overall balance of payments saw a US\$0.7 billion deficit, suggesting close to zero financial account inflows.

Vietnam:

Data releases and forecasts

Week of March 1 – 5

No data releases.

Review of past week's data

No data releases.

Source: Central Bureau of Statistics, Indonesia; Department of Statistics, Malaysia Coordination Board and National Statistics Office, Philippines; Singapore Statistics Department, Office for Industrial Economics, Thailand; Bank of Thailand; General Statistics Office of Vietnam; J.P. Morgan forecasts

India

- **4Q20 GDP growth surprised to the downside, coming in at 0.4%oya, but sequential growth still strong**
- **4Q GDP 96% of the pre-pandemic level**
- **Expecting growth to slow progressively from here**
- **We project GDP growth at -8.0%oya for FY21 and 13.2% for FY22**

4Q20 GDP growth disappointed at 0.4%oya, underpinned by weak service sector growth. Despite the downside surprise, the sequential growth was strong at 25%q/q, saar, taking GDP to 96% of its 1Q20 pre-pandemic level. From here, however, we expect momentum to slow gradually and we now forecast 11%q/q, saar for 1Q21 and an average 5.5%q/q, saar for next year. On a yearly basis, we forecast an 8%y/y contraction in FY21 (year ending March 2021) and 13.2% in FY22 (earlier -6.5% and 13.6%).

India's GDP surprised to the downside, underscoring a divergent recovery

India's 4Q20 GDP growth printed at 0.4%oya, below our expectations. The downside surprise was both because (i) trade, hotels, transport, and communication services continued to contract, much more than some of the formal sector indicators had suggested, indicating continued weakness in the informal sector; and because (ii) government consumption continued to contract, despite a material pickup in central government spending, suggesting contractions in state government spending offset the central government impulse (Table 1).

Table 1: Composition of GDP growth

% oya

	Mar-20	Jun-20	Sep-20	Dec-20
GDP	3.0	-24.4	-7.3	0.4
GVA	3.7	-22.4	-7.3	1.0
Core GVA	1.9	-29.1	-8.5	0.7
Agriculture	6.8	3.3	3.0	3.9
Industry	-2.2	-35.9	-3.0	2.7
- Mining	-0.9	-18.0	-7.6	-5.9
- Manufacturing	-4.2	-35.9	-1.5	1.6
- Electricity	2.6	-9.9	2.3	7.3
- Construction	0.7	-49.4	-7.2	6.2
Services	6.4	-21.4	-11.3	-1.0
- Trade, transport	5.7	-47.6	-15.3	-7.7
- Finance & real estate	4.9	-5.4	-9.5	6.6
- Public administration	9.6	-9.7	-9.3	-1.5

Source: MoSPI

More generally, however, the state of the recovery is best captured by studying the sequential momentum of activity. Despite the downside surprise, growth momentum remained

relatively strong in 4Q20. Recall, 2Q20 had witnessed a 68% ar sequential contraction. On that depressed base, the economy bounced back 119% ar in 3Q, and grew another 25% in 4Q20. Consequently, seasonally-adjusted GDP in 4Q was about 96% of its 1Q20 pre-pandemic level.

Full-year GVA growth marked up but GDP marked down

After this week's downside surprise, the National Statistics Office (NSO) marked down its full-year GDP contraction to 8%y/y from its earlier forecast of -7.7y/y. Prima facie, this is surprising because it suggests activity is weaker than previously envisioned and, more importantly, implies 1Q21 GDP will contract 1.1%oya, which is at odds with the vast majority of high frequency data in the current quarter.

The mystery, however, is solved by looking at the large wedge between GDP and gross value added (GVA). FY21 GVA growth has actually been marked up from -7.2%y/y last month to -6.5%—exactly in line with our GDP forecast. Instead GDP (which is the sum of GVA and net indirect taxes) has been marked down because net indirect taxes and subsidies are now estimated to have plunged 23% versus a -13% initial estimate. Therefore, while GVA growth is stronger than previously envisioned (based on high-frequency data) the net indirect tax adjustment is even larger resulting in GDP growth being marked down in FY21.

2021 growth: signal versus noise; pushes versus pulls

With FY21 growth water under the bridge, the focus will be on how activity evolves in 2021-22. Year-on-year growth rates will be very strong because of very favorable base effects that are likely to mask the underlying growth momentum. For example, even if the seasonally-adjusted level of activity was held constant at our forecasted 1Q21 levels for all of FY22 (there is no sequential growth for four quarters) full-year FY22 growth would print at 9.2%y/y. Our baseline forecast is for 13% full-year growth, but this still implies sequential momentum continuing to slow, and averaging about 5.5%q/q, saar in FY22. If our growth forecasts are realized, activity would still be about 6% below its pre-pandemic path by the end of 2022. It's important, therefore, not to get lulled into complacency by the strong year-on-year growth prints, but instead to focus on underlying momentum.

While India's exports are likely to benefit from stronger global growth in 2021 (JPM forecasts almost 8% annualized global GDP growth over the next two quarters) this will be accompanied by at least two global headwinds. First is the negative terms of trade shock from higher crude oil prices. If crude stabilizes at the current price around US\$65/barrel that would

still constitute an almost 50% increase over the FY21 average, and serve as negative supply shock that simultaneously weighs on activity and pushes up prices. The second is the tightening of domestic financial conditions and its feedback on domestic activity, with domestic bond yields moving up by 40-80bp over the last two months (albeit off depressed levels), both on account of the domestic normalization and firming developed market bond yields. Finally, much will depend on the fiscal stance for next year and whether policymakers can pull off the asset monetization to ensure public capex is not cut. All this, of course, presumes India can stave off any second wave of the virus.

A divergent recovery from COVID-19

Forecasts for next year apart, the 4Q GDP print underscores the divergent nature of India's recovery from COVID-19.

- The divergence between industry and services (which is more contact-intensive): Industry is at producing at 98% of its pre-pandemic level while trade, transport and communications services are at 90% of pre-pandemic levels
- The divergence between the formal and informal sectors: While the profits of larger listed company remained strong in 4Q20, manufacturing growth underwhelmed at just 1.6%oya, suggesting weakness among smaller firms and the informal sector. This message also comes through when considering that GST collection (a proxy for the formal sector) grew 8%oya in the quarter while Core GVA nominal growth was less than half of that at 3.5%oya, suggesting much lower informal sector growth
- The divergence between central and state spending: The CSO press release confirmed that central government spending (net of interest and subsidies) had grown 17% in the quarter in nominal terms (about 12% in real terms). Nevertheless, government consumption contracted again, suggesting a steep fall in state spending, rendering it procyclical
- The divergence in consumption at the top and bottom end of the income spectrum: We had previously spoken about a K-shaped recovery with households at the top of the income pyramid likely to have seen their incomes protected, and savings rates forced up during the lockdown, increasing "fuel in the tank" to drive future consumption. Meanwhile, households at the bottom are likely to have witnessed permanent hits to jobs and incomes, which will hurt their consumption. These cleavages persisted. Over the last four months (October-January) passenger vehicle registrations (proxying upper-end consumption) grew 8% while registrations of two-wheelers fell 10%.

While these divergences are not unique to India, they will need to be carefully managed to ensure the recovery from COVID-19 continues in the coming quarters.

Data releases and forecasts

Week of March 1 – 6

Mon Mar 1	Manufacturing PMI				
	Index	Nov	Dec	Jan	Feb
	Index	56.3	56.4	57.7	-

Review of past week's data

GDP (Feb 26)

% oya	1Q20	2Q20	3Q20	4Q20
% oya	3.0	-24.4	-7.3	0.4
% q/q, saar	15.9	-68.5	118.9	24.7

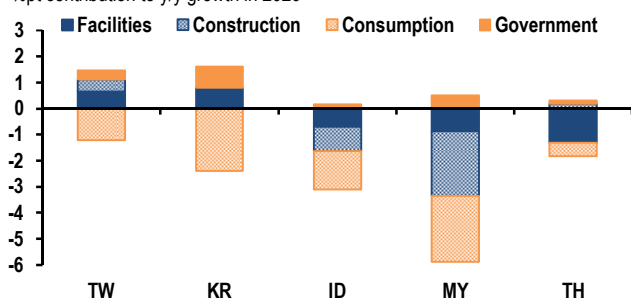
Source: Central Statistical Organization, RBI, Ministry of Commerce, IHS-Markit, and J.P. Morgan forecasts

Asia focus: Capex trends

GDP contracted in 2020 in most of EM Asia in the face of COVID-19. With the virus impacting all economies indiscriminately, details of the expenditure components were similar: private consumption weakened amid distancing efforts while government spending provided buffers, and both exports and imports shrank as a result of reduced global trade. However, growth in facilities investment distinguished North Asia from South East Asia, increasing in Taiwan and Korea but decreasing in ASEAN (Figure 1).

Figure 1: Contribution to GDP growth - domestic demand

%pt contribution to y/y growth in 2020

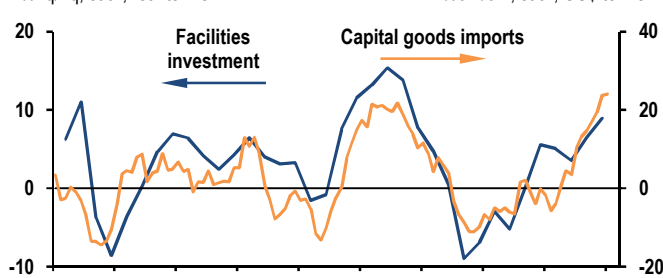


Source: National sources, J.P. Morgan

Figure 2: Korea fixed investment and capital goods imports

%2q/2q, saar, real terms

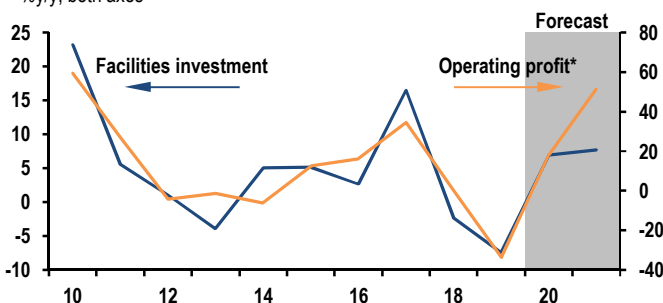
%6m/6m, saar, US\$ terms



Source: National sources, J.P. Morgan

Figure 3: Korea fixed investment and business operating profit

%y/y, both axes



Source: BoK, and J.P. Morgan forecast * KOSPI200, JPM coverage

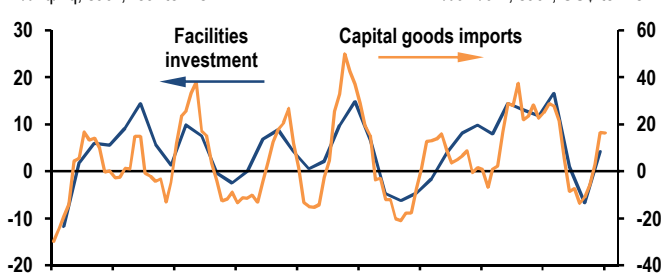
In Korea, facilities investment was notably vigorous in 2020 despite COVID-19 (Figure 2). Business spending was supported by a rebound in operating profit from 2019's low base (Figure 3), and robust demand for Korea's key tech products also boosted profitability of its industry, likely stimulating investment. Investment growth steadily accelerated toward end-2020, and we expect it to maintain the momentum this year based on the global capex recovery.

Taiwan started the year 2020 with strong investment growth, maintaining its momentum since 2019, as producers have re-shored their facilities to Taiwan in recent years. Resilient tech demand has also backed up investment in Taiwan, as it has done in Korea. After taking a slight dip in the middle of the year, Taiwan's facilities investment picked up rapidly in 4Q20, bringing its annual growth into positive territory (Figure 4).

Figure 4: Taiwan fixed investment and capital goods imports

%2q/2q, saar, real terms

%6m/6m, saar, US\$ terms



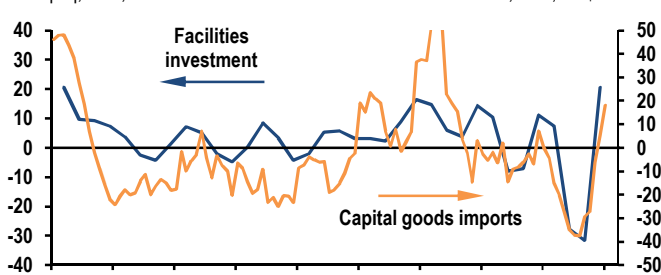
Source: National sources, J.P. Morgan

In Indonesia, facilities investment plummeted during COVID-19's initial wave peak in the middle of 2020, likely because the pandemic weighed heavily on business sentiment. Recovery followed in the latter half of the year but was not enough to fully offset the early plunge so the full-year investment was lower than a year ago. That said, December capital goods imports rose faster than expected, and are worth watching as a barometer of the capex cycle (Figure 5).

Figure 5: Indonesia fixed investment and capital goods imports

%2q/2q, saar, real terms

%6m/6m, saar, US\$ terms



Source: National sources, J.P. Morgan

US economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
1 Mar Manufacturing PMI (9:45am) Feb final <u>58.5</u> ISM manufacturing (10:00am) Feb <u>59.0</u> Construction spending (10:00am) Jan <u>0.8%</u> New York Fed President Williams speaks (9:00am) Fed Governor Brainard speaks (9:05am) Atlanta Fed President Bostic speaks (2:00pm)	2 Mar Light vehicle sales Feb <u>15.6mn</u> Fed Governor Brainard speaks (1:00pm) San Francisco Fed President Daly speaks (2:00pm)	3 Mar ADP employment (8:15am) Feb Services PMI (9:45am) Feb final <u>59.0</u> ISM services (10:00am) Feb <u>58.5</u> Beige book (2:00pm) Philadelphia Fed President Harker speaks (10:00am) Chicago Fed President Evans speaks (1:00pm)	4 Mar Initial claims (8:30am) w/e Feb 27 <u>750,000</u> Productivity and costs (8:30am) 4Q rev <u>-4.7%</u> Unit labor costs <u>6.1%</u> Factory orders (10:00am) Jan <u>3.4%</u> Announce 10-year note (r) <u>\$38bn</u> Announce 30-year bond (r) <u>\$24bn</u> Announce 3-year note <u>\$58bn</u> Fed Chair Powell speaks (12:05pm)	5 Mar Employment (8:30am) Feb <u>200,000</u> Unemployment rate <u>6.3%</u> Average weekly hours <u>34.8</u> International trade (8:30am) Jan <u>-\$67.6bn</u> Consumer credit (3:00pm) Jan
8 Mar Wholesale trade (10:00am) Jan	9 Mar NFIB survey (6:00am) Feb Auction 3-year note <u>\$58bn</u>	10 Mar CPI (8:30am) Feb Federal budget (2:00pm) Feb Auction 10-year note (r) <u>\$38bn</u>	11 Mar Initial claims (8:30am) w/e Mar 6 JOLTS (10:00am) Jan Announce 10-year TIPS (r) <u>\$13bn</u> Announce 20-year bond (r) <u>\$24bn</u> Auction 30-year bond (r) <u>\$24bn</u>	12 Mar PPI (8:30am) Feb Consumer sentiment (10:00am) Mar preliminary QSS (10:00am) 4Q
15 Mar Empire State survey (8:30am) Mar TIC data (4:00pm) Jan	16 Mar Retail sales (8:30am) Feb Import prices (8:30am) Feb Business leaders survey (8:30am) Mar Industrial production (9:15am) Feb Business inventories (10:00am) Jan NAHB survey (10:00am) Mar Auction 20-year bond (r) <u>\$24bn</u> FOMC meeting	17 Mar Housing starts (8:30am) Feb FOMC statement and projections (2:00pm) and press conference (2:30pm)	18 Mar Initial claims (8:30am) w/e Mar 13 Philadelphia Fed manufacturing (8:30am) Mar Leading indicators (10:00am) Feb Announce 2-year FRN (r) <u>\$26bn</u> Announce 2-year note <u>\$60bn</u> Announce 5-year note <u>\$61bn</u> Announce 7-year note <u>\$62bn</u> Auction 10-year TIPS (r) <u>\$13bn</u>	19 Mar
22 Mar Existing home sales (10:00am) Feb QFR (10:00am) 4Q	23 Mar Current account (8:30am) 4Q Philadelphia Fed nonmanufacturing (8:30am) Mar New home sales (10:00am) Feb Richmond Fed survey (10:00am) Mar Auction 2-year note <u>\$60bn</u>	24 Mar Durable goods (8:30am) Feb Manufacturing PMI (9:45am) Mar flash Services PMI (9:45am) Mar flash Auction 2-year FRN (r) <u>\$26bn</u> Auction 5-year note <u>\$61bn</u>	25 Mar Initial claims (8:30am) w/e Mar 20 Real GDP (8:30am) 4Q final KC Fed survey (11:00am) Mar Auction 7-year note <u>\$62bn</u>	26 Mar Advance economic indicators (8:30am) Feb Personal income (8:30am) Feb Consumer sentiment (10:00am) Mar final

Source: Private and public agencies and J.P. Morgan. Further details available upon request.

Euro area economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
1 Mar Euro area: PMI mfg final (10:00am) Feb <u>57.7</u> Germany: PMI mfg final (9:55am) Feb <u>60.6</u> CPI 6 states and prelim (2:00pm) Feb <u>%m/m, nsa: 0.5</u> <u>%oya: 1.2</u> <u>HICP (%oya): 1.8</u> <u>Baden Wuerttemberg(%oya): 1.3</u> <u>Bavaria (%oya): 1.3</u> <u>Brandenburg (%oya): 1.4</u> <u>Hesse (%oya): 0.8</u> <u>North-Rhine West (%oya): 1.1</u> <u>Saxony (%oya): 1.1</u> France: PMI mfg final (9:50am) Feb <u>55.0</u> Italy: PMI mfg final (9:45am) Feb CPI prelim (11:00am) Feb <u>0.3%m/m, nsa</u> <u>0.8%oya, nsa</u> <u>HICP: 0.6%oya, nsa</u> Spain: PMI mfg final (9:15am) Feb Belgium: GDP final (11:00am) 4Q	2 Mar Euro area: HICP flash (11:00am) Feb <u>0.8%oya, nsa</u> <u>HICP core: 1.0%oya, nsa</u> Germany: Employment (9:55am) Feb <u>Change (ch m/m, 000s, sa): 0</u> Unemployment (9:55am) Feb <u>Registered (ch m/m, 000s, sa): 0</u> <u>Unempl. rate: 6.0%, sa</u> Retail sales (8:00am) Jan <u>-2.0%m/m</u>	3 Mar Euro area: PMI serv. & comp (10:00am) Feb <u>Services: 44.7</u> <u>Composite: 48.1</u> PPI (11:00am) Jan MFI interest rates (10:00am) Jan Germany: PMI serv. & comp (9:55am) Feb <u>Services: 45.9</u> <u>Composite: 51.3</u> France: Monthly budget situation (8:45am) Jan PMI serv. & comp (9:50am) Feb <u>Services: 43.6</u> <u>Composite: 45.2</u> Italy: PMI serv. & comp (9:45am) Feb GDP final (10:00am) 4Q <u>-2.0%q/q, sa</u> <u>-7.7%q/q, saar</u> <u>-6.6%oya</u> Spain: PMI serv. & comp (9:15am) Feb	4 Mar Euro area: Retail sales (11:00am) Jan <u>-2.3%m/m, sa</u> Unemployment rate (11:00am) Jan <u>8.3%, sa</u> Netherlands: CPI (6:30am) Feb	5 Mar Germany: Mfg orders (8:00am) Jan <u>Total: 0.0%m/m</u> <u>Total ex. bulk orders: 0.0%m/m</u> France: Foreign trade (8:45am) Jan
8 Mar Germany: Industrial production (8:00am) Jan	9 Mar Euro area: Employment final (11:00am) 4Q GDP final (11:00am) 4Q Germany: Foreign trade (8:00am) Jan Italy: Industrial prod. (10:00am) Jan	10 Mar France: Industrial production (8:45am) Jan Italy: PPI (11:00am) Jan	11 Mar Euro area: ECB rate announcement (1:45pm) Mar	12 Mar Euro area: Industrial prod. (11:00am) Jan Germany: CPI final (8:00am) Feb Spain: CPI final (9:00am) Feb HICP flash (9:00am) Feb
15 Mar	16 Mar Germany: ZEW bus. survey (11:00am) Mar France: CPI final (8:45am) Feb Italy: CPI final (10:00am) Feb	17 Mar Euro area: HICP final (11:00am) Feb Car registrations (8:00am) Feb Construction output (11:00am) Jan	18 Mar Euro area: Foreign trade (11:00am) Jan Labor costs (11:00am) 4Q Italy: Foreign trade (10:00am) Jan	19 Mar Germany: PPI (8:00am) Feb
22 Mar Euro area: Balance of Payments (10:00am) Jan Belgium: BNB cons. conf. (11:00am) Mar	23 Mar	24 Mar Euro area: PMI mfg prelim (10:00am) Mar PMI serv. & comp (10:00am) Mar EC cons. Conf. flash (4:00pm) Mar Germany: PMI mfg prelim (9:30am) Mar PMI serv. & comp (9:30am) Mar France: PMI mfg prelim (9:15am) Mar PMI serv. & comp (9:15am) Mar	25 Mar Euro area: M3 money supply (10:00am) Feb Germany: GfK cons. conf. (8:00am) Mar France: INSEE bus. conf. (8:45am) Mar Belgium: BNB bus. conf. (3:00pm) Mar	26 Mar Germany: IFO bus. survey (10:00am) Mar France: INSEE cons. conf. (8:45am) Mar Italy: ISAE bus. conf. (10:00am) Mar ISAE cons. conf. (10:00am) Mar Spain: GDP final (9:00am) 4Q

Highlighted data are scheduled for release on or after the date shown. Times shown are local. Source: Private and public agencies and J.P. Morgan. Further details available upon request.

Japan economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
1 Mar PMI manufacturing final (9:30am) Feb Auto registrations (2:00pm) Feb	2 Mar Job offers to applicants ratio (8:30am) Jan <u>1.04</u> Unemployment rate (8:30am) Jan <u>3.1%</u> Corporate survey (8:50am) 4Q Auction 10-year note	3 Mar PMI services final (9:30am) Feb	4 Mar Consumer sentiment (2:00pm) Feb <u>32.0</u> Auction 30-year note	5 Mar Consumption activity index (2:00pm) Jan Auction 3-month bill
8 Mar Bank lending (8:50am) Feb Current account (8:50am) Jan Economy Watchers' survey (2:00pm) Feb	9 Mar All household spending (8:30am) Jan Employers' survey (8:30am) Jan M2 (8:50am) Feb GDP 2nd (8:50am) 4Q Auction 6-month bill Auction 5-year note	10 Mar	11 Mar Corporate goods prices (8:50am) Feb Auction 20-year note	12 Mar Business Outlook Survey (8:50am) 1Q Auction 3-month bill
15 Mar Private machinery orders (8:50am) Jan Tertiary sector activity index (1:30pm) Jan	16 Mar IP final (1:30pm) Jan Remarks by Governor KURODA at the FIN/SUM 2021	17 Mar Reuters Tankan (8:50am) Mar Trade balance (8:50am) Feb Auction 1-year note	18 Mar Construction spending (2:00pm) Jan BoJ Monetary Policy Meeting Auction 3-month bill	19 Mar Nationwide core CPI (8:30am) BoJ Monetary Policy Meeting BoJ outlook report BoJ governor Kuroda's press conference
During the week: CAO private consumption index Jan (15-19 Mar)				
22 Mar Coincident CI (2:00pm)	23 Mar	24 Mar Corporate service prices (8:50am) Feb PMI manufacturing prelim (9:30am) Feb PMI service prelim (9:30am) Feb Minutes of Jan 20, 21 BoJ Monetary Policy Meeting (8:50am) Auction 6-month bill	25 Mar Auction 40-year note	26 Mar Tokyo core CPI (8:30am) Mar Auction 3-month bill

Times shown are local. Source: Private and public agencies and J.P. Morgan. Further details available upon request.

Canada economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
1 Mar Current account (8:30am) 4Q -C\$7.1bn Markit manufacturing PMI (9:30am) Feb	2 Mar Quarterly GDP (8:30am) 4Q 7.6%.saar Monthly GDP (8:30am) Jan 0.3%	3 Mar Building permits (8:30am) Jan 7.0%	4 Mar Productivity & costs (8:30am) 4Q	5 Mar International trade (8:30am) Jan -C\$1.4bn Ivey PMI (10:00am) Feb 61.0 J.P. Morgan composite 60.5
8 Mar	9 Mar	10 Mar Bank of Canada Rate announcement (10:00am)	11 Mar Deputy Governor Lawrence Schembri speaks before Restaurants Canada by videoconference (1:30pm)	12 Mar Labor Force Survey (8:30am) Feb Wholesale sales (8:30am) Jan New vehicle sales (8:30am) Jan Capacity utilization (8:30am) 4Q National Balance Sheet (8:30am) 4Q
15 Mar Housing starts (8:15am) Feb Manufacturing sales (8:30am) Jan Existing home sales (9:00am) Feb	16 Mar International transactions in securities (8:30am) Jan	17 Mar CPI (8:30am) Feb Teranet/National Bank HP Index (8:30am) Feb	18 Mar New housing price index (8:30am) Feb	19 Mar Retail sales (8:30am) Jan
22 Mar	23 Mar Deputy Governor Toni Gravelle speaks before CFA Society Toronto by videoconference (1:15pm)	24 Mar	25 Mar CFIB Business Barometer Index (6:00am) Mar	26 Mar

Source: Private and public agencies and J.P. Morgan. Further details available upon request. All existing home sales are tentative.

Latin America economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
1 Mar Argentina: Tax Collections Feb <u>2.5%oya</u> Brazil: PMI Manufacturing Feb Trade balance Feb Chile: Economic activity Jan <u>-1.5%oya</u> Mexico: Remittances Jan <u>US\$3.0bn</u> IMEF manufacturing index Feb <u>48.9</u> IMEF nonmanufacturing index Feb <u>46.6</u> Peru: CPI Feb <u>-1.9%oya</u>	2 Mar Brazil: FIPE CPI Feb Mexico: PS budget balance Jan	3 Mar Argentina: Vehicle production Feb Vehicle sales Feb Brazil: GDP 4Q20 <u>10.0%q/q</u> <u>saar: -2.0%oya</u> Uruguay: CPI Feb <u>0.7% m/m; 8.97%oya</u>	4 Mar Argentina: IP Jan <u>4.8%oya</u> Construction Jan <u>28.0%oya</u> Colombia: Exports Jan <u>US\$2.7bn</u>	5 Mar Brazil: IP Jan <u>0.0% m/m; 1.2%oya</u> Chile: Nominal Wage Jan <u>4.0%oya</u> Colombia: CPI Feb <u>0.42% m/m; 1.34%oya</u> Mexico: Auto report Feb GFI Dec <u>1.0% m/m; -11.0%oya</u>
During the week: Brazil: Vehicle sales Feb (4-5 Mar) Brazil: Auto production Feb (4-5 Mar) Chile: IMCE Business confidence Feb (1-5 Mar) <u>56</u>				
8 Mar Brazil: IGP-DI Feb Chile: Trade balance Feb	9 Mar Mexico: Biweekly core CPI Biweekly CPI Core CPI Feb CPI Feb	10 Mar	11 Mar Argentina: CPI Feb Peru: Reference rate Mar Brazil: IPCA Feb	12 Mar Brazil: Retail sales Jan Mexico: IP Jan
During the week: Mexico: ANTAD same-store sales Feb (8-12 Mar) Peru: Trade balance Jan (9-11 Mar)				
15 Mar Colombia: IP Jan Retail sales Jan Peru: Economic Activity Jan National Unemployment rate Feb Uruguay: Industrial production Jan	16 Mar Uruguay: National Unemployment rate Jan	17 Mar	18 Mar Chile: Current Account Balance 4Q GDP 4Q Colombia: Trade balance Jan Economic Activity Jan	19 Mar Mexico: Aggregate supply & demand 4Q
During the week: Uruguay: GDP 4Q (15-19 Mar) Brazil: BCB meeting Mar (17-21 Mar)				
22 Mar Argentina: Budget balance Feb Paraguay: Monetary Policy Rate Mar	23 Mar Argentina: GDP 4Q Brazil: FGV: consumer confidence Mar	24 Mar Mexico: Biweekly core CPI Biweekly CPI Unemployment Feb	25 Mar Brazil: IPCA-15 Mar Mexico: GDP monthly proxy Jan Retail sales Jan Banxico meeting Mar	26 Mar Argentina: Trade balance Feb Brazil: Current Account Feb FDI Feb Mexico: Trade balance
During the week: Brazil: Tax collections Feb (22-25 Mar) Paraguay: GDP 4Q (26-31 Mar) Colombia: Overnight lending rate Mar (26-30 Mar)				

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UK and Scandinavia Calendar

Monday	Tuesday	Wednesday	Thursday	Friday
1 Mar United Kingdom: M4 & M4 lending final (9:30am) Jan Net lending to individuals (9:30am) Jan PMI Mfg final (9:30am) Feb Sweden: PMI Mfg (8:30am) Feb Wage stats (9:30am) Dec Norway: Retail sales (8:00am) Jan PMI Mfg (10:00am) Feb	2 Mar United Kingdom: Nationwide HPI (7:00am) Feb CBI growth indicator (12:01am) Feb	3 Mar United Kingdom: PMI Services final (9:30am) Feb Sweden: Services PMI (8:30am) Feb	4 Mar United Kingdom: New car regs (9:00am) Feb PMI Construction (9:30am) Feb	5 Mar United Kingdom: Trade balance (7:00am) Jan Halifax HPI (8:30am) Feb Sweden: Budget Balance (9:30am) Feb
8 Mar Norway: IP Mfg (8:00am) Jan	9 Mar United Kingdom: BRC retail sales monitor (12:01am) Feb Sweden: Industrial production & orders (9:30am) Jan Household cons. (9:30am) Jan Norway: Monthly GDP (8:00am) Jan Regional network survey (10:00am) 1Q	10 Mar Norway: CPI (8:00am) Feb PPI (8:00am) Feb	11 Mar United Kingdom: RICS HPI (12:01am) Feb Sweden: PES unemployment (6:00am) Feb	12 Mar United Kingdom: Monthly GDP (9:30am) Jan Index of services (7:00am) Jan Industrial production (7:00am) Jan Trade balance (7:00am) Jan BoE/NOP Inflation attitudes survey (9:30am) Feb
15 Mar United Kingdom: Rightmove HPI (12:01am) Mar Sweden: CPI (9:30am) Feb Norway: Trade balance (8:00am) Feb	16 Mar	17 Mar	18 Mar United Kingdom: MPC rate announcement and asset purchase target (12:00pm) Mar Norway: Norges Bank rate announcement (10:00am) Mar	19 Mar United Kingdom: Gfk cons. conf. (12:01am) Mar Public sector finances (7:00am) Feb Norway: Building statistics (10:00am) Feb
During the week: CBI industrial trends Mar (18-24 Mar)				
22 Mar	23 Mar United Kingdom: Labor market report (7:00am) Feb	24 Mar United Kingdom: CPI (7:00am) Feb ONS HPI (9:30am) Jan PMI Mfg prelim (9:30am) Mar PMI Services prelim (9:30am) Mar	25 Mar Sweden: Household lending (9:30am) Feb PPI (9:30am) Feb	26 Mar United Kingdom: Retail sales (7:00am) Feb Car manufacturing (12:01am) Feb Sweden: Retail sales (9:30am) Trade balance (9:30am) Norway: Credit indicator growth (8:00am) Labor directorate unemployment (10:00am)
During the week: CBI distributive trades Mar (24-28 Mar)				

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Emerging Europe/Middle East/Africa economic calendar

Monday	Tuesday	Wednesday	Thursday	Friday
1 Mar Czech Republic: PMI (9:30am) Feb Hungary: PMI (9:00am) Feb Poland: PMI (9:00am) Feb Russia: Manufacturing PMI (9:00am) Feb 52.0 Turkey: GDP (9:00am) 4Q PMI (9:00am) Feb South Africa: Vehicle sales Feb Barclays PMI (11:00am) Feb	2 Mar Czech Republic: GDP prelim (9:00am) 4Q 1.2% q/q.saar Hungary: GDP final (9:00am) 4Q 4.5%q/q.saar PPI (9:00am) Jan	3 Mar Poland: NBP rate decision Mar On hold: 0.10% Turkey: CPI (9:00am) Feb 15.2%oya Nigeria: PMI (8:45am) Feb	4 Mar Hungary: Retail sales (9:00am) Jan Trade balance final (9:00am) Dec EUR310mn Romania: Retail sales (9:00am) Jan Ukraine: NBU rate decision (2:00pm) Mar On hold: 6.00%	5 Mar Hungary: Industrial output (9:00am) Jan Russia: CPI (7:00pm) Feb 5.5%oya South Africa: Gross reserves (8:00am) Feb
During the week: Kazakhstan: CPI Feb (2-4 Mar)				
8 Mar Czech Republic: Average real wage (9:00am) 4Q Israel: Current account (1:00pm) 4Q	9 Mar Czech Republic: Trade balance (9:00am) Jan Hungary: CPI (9:00am) Feb Romania: GDP prelim (9:00am) 4Q South Africa: GDP (11:30am) 4Q Ukraine: CPI (3:30pm) Feb Kazakhstan: NBK rate decision (3:00pm) Mar	10 Mar Czech Republic: CPI (9:00am) Feb Turkey: Unemployment (9:00am) Dec Israel: GDP prelim (1:00pm) 4Q Ghana: CPI Feb Egypt: CPI Feb	11 Mar Hungary: Trade balance (9:00am) Jan Romania: CPI (9:00am) Feb Turkey: Current account (9:00am) Jan South Africa: Current account and Quarterly Bulletin (11:00am) 4Q Serbia: NBS rate decision (12:00pm) Mar	12 Mar Czech Republic: Industrial output (9:00am) Jan Romania: Industrial output (9:00am) Jan Trade balance (9:00am) Jan Russia: Foreign trade (4:00pm) Jan Turkey: Industrial output (9:00am) Jan
During the week: South Africa: Retail sales Jan (11-17 Mar) South Africa: Manufacturing output Jan (11-17 Mar) South Africa: BER consumer confidence 4Q (11-31 Mar)				
15 Mar Czech Republic: PPI (9:00am) Feb Retail sales (9:00am) Jan Poland: CPI (10:00am) Feb Israel: CPI (6:30pm) Feb	16 Mar Czech Republic: Current account (10:00am) Jan Poland: Core inflation (2:00pm) Feb Current account (2:00pm) Jan Romania: Current Account Jan Russia: Industrial output (7:00pm) Feb	17 Mar Poland: Average gross wages and Em- ployment (10:00am) Feb Russia: PPI (7:00pm) Feb Mozambique: CBM rate decision Mar	18 Mar Poland: Industrial output (10:00am) Feb PPI (10:00am) Feb Turkey: CBRT rate decision (1:00pm) Mar Egypt: CBE rate decision Mar	19 Mar Poland: Retail sales (10:00am) Feb Russia: CBR rate decision (1:30pm) Mar Retail sales, Unemployment & Investment (7:00pm) Feb
During the week: Saudi Arabia: CPI Feb (15-16 Mar) Angola: CPI Feb (16-27 Mar) Poland: Budget balance Feb (17-31 Mar)				
22 Mar Ghana: BOG rate decision Mar Ukraine: GDP final (3:30pm) 4Q	23 Mar Hungary: Current account (8:30am) 4Q NBH rate decision (2:00pm) Mar Poland: Unemployment (10:00am) Feb Nigeria: CBN rate decision Mar	24 Mar Czech Republic: CNB rate decision (2:30pm) Mar South Africa: CPI (10:00am) Feb	25 Mar South Africa: SARB rate decision Mar Zambia: CPI Feb	26 Mar Turkey: Capacity utilization (9:00am) Mar

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Global Data Diary

Week / Weekend	Monday	Tuesday	Wednesday	Thursday	Friday
27 Feb - 5 Mar	1 March	2 March	3 March	4 March	5 March
China • FX reserves (Feb)	Germany • CPI (Feb) Korea • Trade balance (Feb) Turkey • GDP (4Q) United States • ISM mfg (Feb)	Australia • RBA mtg: no chg Canada • GDP (4Q) Czechia • GDP (4Q) Euro area • CPI (Feb) Germany • Retail sales (Jan) • U-rate (Feb) Japan • U-rate (Jan) Korea • IP (Feb) United States • Light vehicle sls (Feb)	Australia • GDP (4Q) Brazil • GDP (4Q) Poland • NBP mtg: no chg Turkey • CPI (Feb) United States • ADP employment (Feb) • ISM non-mfg (Feb) Global • All-industry PMI (Feb)	Euro area • Retail sales (Jan) • U-rate (Jan) Japan • Consumer sent (Feb) Korea • CPI (Feb) Malaysia • BNM mtg: no chg United Kingdom • New car regs (Feb) United States • Factory orders (Jan) • Prod & costs (4Q, rev)	Brazil • IP (Jan) Germany • Mfg orders (Jan) Japan • CAI (Jan) United Kingdom • Trade balance (Jan) United States • Consumer credit (Jan) • Labor mrkt report (Feb) • Trade balance (Jan)
6 - 12 March	8 March	9 March	10 March	11 March	12 March
China • Money supply/TSF (Feb)	Germany • IP (Jan) Japan • Econ wtchrs srvy (Feb) United States • Wholesale trade (Jan)	Euro area • GDP (4Q, fnl) Germany • Trade balance (Jan) Japan • GDP (4Q, 2 nd est) Mexico • CPI (Feb) Romania • GDP (4Q) South Africa • GDP (4Q) Taiwan • CPI (Feb) • Trade balance (Feb) United States • NFIB srvy (Feb)	Canada • BOC mtg: no chg China • CPI (Feb) Israel • GDP (4Q) United States • CPI (Feb)	Brazil • CPI (Feb) Euro area • ECB mtg: no chg Peru • BCRP mtg: no chg United States • JOLTS (Jan)	Brazil • Retail sales (Jan) Euro area • IP (Jan) India • CPI (Feb) • IP (Jan) Mexico • IP (Jan) Russia • Trade balance (Jan) Turkey • IP (Jan) United Kingdom • IP (Jan) • Trade balance (Jan) United States • PPI (Feb) • QSS (4Q) • UMich cons snt (Mar, prl)

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Economic Research**Global Data Watch**

February 26, 2021

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Economic Research**Global Data Diary**

February 26, 2021

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